Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

TOUCHE ROSS & CO.,
Petitioner,

v.

CONGREGATION OF THE PASSION,
HOLY CROSS PROVINCE,
Respondent.

Petition for a Writ of Certiorari to the Supreme Court of Illinois

PETITION FOR A WRIT OF CERTIORARI

FRANCIS J. HIGGINS
(Counsel of Record)
JOHN J. VERSCAJ
BELL, BOYD & LLOYD
Three First National Plaza
70 West Madison Street
Chicago, Illinois 60602
(312) 372-1121

Attorneys for Petitioner
Touche Ross & Co.

169 pp

QUESTIONS PRESENTED

(1) Whether a state court may deny collateral estoppel effect to alternative determinations made by a federal court in prior federal question litigation between the parties, where each such determination independently supported the federal judgment and each was reviewed and affirmed on appeal?

(2) Whether a state court may limit the collateral estoppel effect of a federal judgment to the plaintiff's "theories of recovery" in subsequent state court litigation?

PARTIES TO THE PROCEEDING

Petitioner Touche Ross & Co., the defendant-appellant below, is an accounting firm organized as a partnership. Respondent Congregation of the Passion, Holy Cross Province, the plaintiff-appellee below, is a not-for-profit corporation and an order of the Catholic Church. It has no parent companies or subsidiaries.

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TOUCHE ROSS & CO.,
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CONGREGATION OF THE PASSION,
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Respondent.

Petition for a Writ of Certiorari to the Supreme Court of Illinois

PETITION FOR A WRIT OF CERTIORARI

Touche Ross & Co. ("Touche Ross") respectfully petitions that a writ of certiorari issue to review the decision of the Supreme Court of Illinois in *Congregation of the Passion, Holy Cross Province* v. *Touche Ross & Co.*, 159 Ill. 2d 137, __ N.E.2d ___ (1994), *reh'g denied*, in which a divided court refused to give collateral estoppel effect to determinations made in prior federal litigation between the same parties on the same facts and affirmed a $3.89 million judgment for respondent contrary to those prior federal determinations.

OPINIONS BELOW

The opinion of the Illinois Supreme Court is reported at 159 Ill. 2d 137, __ N.E.2d ___ (1994) and is reproduced in Appendix A. The opinion of the Illinois Appellate Court is reported at 224 Ill. App. 3d 559, 586 N.E.2d 600 (1991), and is reproduced in Appendix B. The unreported opinions of the United States District Court for the Northern District of Illinois are reproduced in Appendices C and D. The opinion of the Seventh Circuit affirming the district court is reported at 800 F.2d 177 (7th Cir. 1986) and is reproduced in Appendix E.

JURISDICTION

The opinion of the Illinois Supreme Court was issued on April 21, 1994. (App. A.) A timely petition for rehearing was denied on May 27, 1994. (App. F.) This Court has jurisdiction to review the judgment of the Illinois Supreme Court by writ of certiorari in that a state court's disregard of a decree of a court of the United States raises a federal question reviewable under 28 U.S.C. § 1257(a).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Article I, § 8, cl. 18, Article III, § 1, Article III, § 2, cl. 1, and Article VI, cl. 2 of the Constitution of the United States, and Section 5/2-1303 of the *Code of Civil Procedure of Illinois,* 735 ILCS 5/2-1303, are reproduced in Appendix G.

STATEMENT OF THE CASE

This case was brought in the Circuit Court of Cook County, Illinois by respondent Congregation of the Passion, Holy Cross Province (the "Congregation"), in order to relitigate issues

resolved against it in prior federal securities fraud litigation.[1] Both the federal and state court litigations arose out of the Congregation's engagement of Touche Ross to perform unaudited reviews of the Congregation's financial statements for the fiscal years 1976 through 1980, and both litigations were based upon the same allegations that Touche Ross had made misrepresentations to the Congregation in accounting reports.[2] The Illinois trial and appellate courts declined, for different and inconsistent reasons, to give collateral estoppel effect to the federal determinations. In affirming the judgment of the Illinois Appellate Court, the Illinois Supreme Court applied restrictive *state* law preclusion principles notwithstanding the fact that the federal judgment was entered in an action based upon federal question jurisdiction.

A. The Congregation's Arbitrage Losses.

The Congregation is a Catholic religious order. In 1975 it created a $1 million "retirement fund" for its members and in 1976 a $1 million "permanent fund" for educational purposes. The Congregation's Business Advisory Board (the "BAB"), a lay advisory board of businessmen and experienced traders, provided investment and general business advice to the Congregation concerning these funds. (R.P. 2827-29.) The Congregation sought an above-market annual return of 12-15% on its fund

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[1]Exhibits submitted by the plaintiff and defendant in the state court trial are referred to herein as "(PX __)" and "(DX __)," respectively. Other documents filed in the trial court and included in the record on appeal to the Illinois Supreme Court are referred to herein as "(C. __)." The Report of Proceedings before the Illinois trial court is referred to herein as "(R.P. __)." For ease of reference, certain factual matters established in the federal proceedings are cited to the Seventh Circuit's decision reported at 800 F.2d 177 (7th Cir. 1986).

[2]A "review" engagement, unlike an audit, consists principally of inquiries to management personnel. (DX 198.) It does not contemplate the accountant's expression of an opinion with respect to the financial statements reviewed, and Touche Ross never expressed an opinion on the financial statements in question. (DX 271 at 5-6; DX 200 at 1, 3.)

investments. (DX 39, 120; R.P. 1169-70, 1245-46, 1531, 1539-40.)

In an attempt to achieve its above-market investment expectations, the Congregation retained Cranford D. Newell ("Newell") as its investment manager and in fiscal year 1976 committed the Congregation's "retirement" and "permanent" funds to Newell's full discretionary investment authority. (DX 45.) Newell, with the approval of the Congregation, invested the "retirement" and "permanent" funds in *arbitrage* transactions in government securities.[3] The Congregation "was fully aware of the transactions and the type of risks involved." (800 F.2d at 184; App. E-13.) The BAB monitored the Newell arbitrage activities, as did the Congregation's own officers. (800 F.2d at 179; App. E-4.)

Until May of 1981, Newell exercised his discretion to take arbitrage positions on behalf of the Congregation with over 30 broker-dealers. (800 F.2d at 179; App. E-3.) The periodic reports that Newell submitted to the Congregation reflected open arbitrage positions at what Newell called "margin," *i.e.,* net cash paid, *not* at the market value of the securities. (R.P. 1542-43, 1727.) The Congregation at all times recorded the positions in its financial records on the same basis. (R.P. 1721, 2414-16.)

The accounting treatment of the Newell open arbitrage positions in the Congregation's unaudited financial statements was discussed by the Congregation and Touche Ross during Touche Ross' review of the financial statements for the year ended June 30, 1976 (the year in which the Newell arbitrage investments were first made) and the joint decision was made to report the Newell open arbitrage positions in the annual financial statements at "margin," *i.e.,* net cash paid. (800 F.2d at 179; App. E-4; R.P. 1735-36; *see also* R.P. 116-17, 1662-63, 3962-63, 3974.) As a consequence, "[e]ach year, a footnote

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[3]The dissent in the Illinois Supreme Court characterized the arbitrage investments as "big time gambling" by the Congregation. (159 Ill. 2d at 176; App. A-33.)

appeared in the report indicating that the arbitrage investments were not reported at current market value; instead '[o]nly the required margin payments were carried as investments.'" (800 F.2d at 179; App. E-4; *see also* R.P. 1157-58, 3434-36, 3803, 3864-65, 3973-74.)

Members of the BAB became aware of large *realized* losses in Newell's accounts and in 1977 considered whether Newell should be terminated or his arbitrage trading halted. (DX 122 at 2, 3; R.P. 988-90.) The Congregation chose to continue its relationship with Newell notwithstanding the losses.[4]

During its review of the Congregation's June 30, 1980 unaudited financial statements, Touche Ross raised a question concerning a $3.6 million balance which Newell had reported to the Congregation. Touche Ross was provided with information indicating that there was an unrealized loss of $2.4 million in the accounts as of June 30. (DX 266-68; R.P. 4001-03, 4010-18.) In early February, 1981 Newell confirmed that loss to both Touche Ross and the Congregation. (R.P. 2066-29, 2909-11, 4020-21.) *Despite knowledge of the $2.4 million loss, the Congregation took no action to terminate arbitrage trading, to close the accounts, or to transfer the management of the accounts to someone other than Newell.* (800 F.2d at 180; App. E-4.) Rather than liquidating the accounts, the Congregation decided in April 1981, to invest *an additional $500,000* with Newell. (800 F.2d at 180; App. E-4; R.P. 772-73, 2526, 2937, 947-48.) Only in May 1981, when the equity in the Newell-managed accounts had been depleted, did

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[4]The Seventh Circuit found:

> As early as 1976, members of the Business Advisory Board of the Holy Cross Province (Board) expressed some concern not only about the high risk involved in the arbitrage transactions but also about the pressure that the high expectations of return placed on Mr. Newell .... The Board solicited a study of Mr. Newell's investments. An independent firm concluded that Mr. Newell had taken substantial risks in a period of uncertainty in the bond market. (800 F.2d at 179; App. E-4.)

the Congregation close the accounts. (800 F.2d at 180; App. E-4; R.P. 1586-88, 2503.)

B. The Federal Litigation.

In 1981, the Congregation sued Newell and four government bond broker-dealers in the district court, alleging federal securities law violations. (C. 10250-70.) The dealers counterclaimed for amounts owed by the Congregation after liquidation of the Newell accounts. In 1982, the Congregation joined Touche Ross as an additional defendant and charged it with aiding and abetting Newell's alleged securities law violations by issuing misleading financial reports to the Congregation which reported the arbitrage investments at "margin," failing to report the market value of the arbitrage investments, and thereby assertedly misrepresenting the value of the positions and concealing unrealized losses in the Newell positions. (C. 16-41.) The Congregation alleged that if Touche Ross had not issued misleading financial reports, the Congregation would have learned of the losses and would have terminated Newell's trading. (C. 37.) The Congregation's amended federal complaint also contained "pendent" state law claims based on the same factual allegations.

In September 1984, the district court granted summary judgment motions filed by Touche Ross and the broker-dealers. (App. C.) Based on an extensive discovery record, the district court held that: (a) the broker-dealers had not violated the securities laws because the Congregation's complete delegation of authority to Newell placed the transactions outside the "purchase or sale" requirement of Section 10(b) of the Securities Exchange Act of 1934 *and* because the defendants had made no misrepresentations or actionable omissions; (b) as a consequence, there were no primary securities law violations by Newell that Touche Ross could have aided or abetted; and (c) "additionally," there was "no evidentiary basis" for the allegations that Touche Ross had made "misrepresentations" or had aided and abetted Newell in any way. (C. 713-24; App. C-3-6.) In reaching its decision, the district court also made specific findings that the defendants had made no misrepresentations to the Congregation; that Newell was

the Congregation's agent acting within the scope of his authority; that the Congregation was able to track and understand the Newell transactions; and that the Congregation's reliance was on Newell, not on the defendants. (C. 713-24; App. C-3-6.)

The district court subsequently entered summary judgment for the broker-dealer defendants on counterclaims seeking recovery of amounts due on the Congregation's accounts. (C. 287-299; App. D.) In its decision on the counterclaims, the district court relied upon its earlier findings and found, in addition, that the Congregation's decision to continue trading through Newell until May 1981 was made "in the face" of bank statements and other information available to the Congregation, including confirmation slips and "accurate reports of the transactions" supplied by the broker-dealers. (C. 291-294; App. D-5-6.)

The Seventh Circuit affirmed both summary judgment rulings on all grounds. Like the district court, the Seventh Circuit divided its opinion into alternative holdings that: (a) there were no primary securities laws violations by the brokers or Newell; (b) therefore Touche Ross could not have "aided and abetted" Newell; and (c) "[m]oreover," there "was no evidentiary basis" for the allegations that Touche Ross had aided and abetted Newell by misrepresenting the investments in erroneous reports. (800 F.2d at 180-84; App. E-6-13.) The Seventh Circuit also affirmed each of the district court's specific determinations, finding that Newell was the Congregation's agent; that the Congregation understood and was warned about the Newell transactions; that Touche Ross had consulted with the Congregation concerning the reporting of the investments and that it was decided to report the investments at cost; that the Congregation's own financial statements *expressly stated that the arbitrage investments were not reported at market value;* that *Touche Ross made no misrepresentations to the Congregation;* and that the Congregation was informed of Newell's losses *in February* 1981 but nevertheless *thereafter* invested an additional $500,000 with him. (800 F.2d at 179, 183-84; App. E-3-4, 11-14.) The Seventh

Circuit concluded that the Congregation was responsible for its own losses:

> *The Congregation granted Mr. Newell full authority to enter into these transactions; it was fully aware of the transactions and the type of risks involved. It must now be responsible for the deficit created when the investments lost money.* (800 F.2d at 184; App. E-13.) (Emphasis supplied.)

C. The State Court Litigation.

In late 1984, while the federal action was still pending, the Congregation sued Touche Ross for a second time—this time in the Circuit Court of Cook County, Illinois—on state law claims sounding in negligence and breach of contract. The state court complaint was based upon the same alleged facts and transactions as the Congregation's federal court suit. (C. 2-15.)[5] Again, as in the federal litigation, the Congregation alleged that Touche Ross should have reported the Newell positions at market value, that the Congregation believed that Touche Ross' reports had done so, but that in fact Touche Ross had reported the Newell positions at "cost" or "margin"—thus making the investments appear profitable when in fact there were unrealized losses in the Newell accounts. (C. 8-10.) *Again,* as in the federal litigation, the Congregation's theory of proximate causation was that, if Touche Ross had reported the positions to plaintiff at market value, the unrealized losses would have been disclosed to the Congregation

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[5]As the dissent in the Illinois Supreme Court put it:

> After the adverse ruling in Federal district court, the plaintiff refiled its complaint against Touche Ross in the circuit court of Cook County. The complaint was based upon the same facts and transactions as were the subject of the Congregation's Federal lawsuit. (159 Ill. 2d at 179; App. A-36.)

and it supposedly would have ended or curtailed Newell's arbitrage investments.[6] (R.P. 4678-79, 4693.)

Touche Ross unsuccessfully moved to dismiss and for summary judgment on the ground that the federal determinations precluded the Congregation from relitigating issues essential to its state law claims. (C. 704-11, 1415-1423, 8364-71, 8394.)[7] It also filed a motion *in limine* seeking an order precluding the Congregation from introducing evidence contradicting the findings of fact of the federal courts, but the trial court denied that motion and instead granted the Congregation's motion to preclude *Touche Ross* from referring to the federal litigation at trial. (C. 9331-9341; 10314.) The trial court's response to the parties' motions in limine revealed disdain for the federal courts' determinations and for federal courts in general:

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[6]After filing its state court action, the Congregation was clearly concerned about the collateral estoppel effect of the district court's findings and sought a "clarification" of the district court's summary judgment rulings as to Touche Ross. The district court declined "to alter the scope of its rulings" and rejected the Congregation's argument that its statements concerning Touche Ross lacked a "substantial factual basis." (C. 282-84.)

[7]Touche Ross specifically sought dismissal on the ground that:

> The doctrine of collateral estoppel precludes the plaintiff from relitigating the findings of the federal district court and the Seventh Circuit that (1) the plaintiff relied on its own investment advisor, Newell, to make the investment decisions at issue; (2) the investments were tracked by the plaintiff's officers and other advisors; (3) the plaintiff understood the risks involved in making those investments; (4) Touche Ross consulted the Congregation concerning the manner in which the arbitrage investments would be reported and it was decided to report them at cost; and (5) each report expressly disclosed that the arbitrage investments were not reported at their current market value. (C. 709-10.)

Touche Ross' summary judgment motion similarly urged the trial court to give "preclusive collateral estoppel effect" to the federal determinations. (C. 8370.)

> [T]hey [the federal courts] have been known to err quite a bit. In fact, they make their own law over there. As a matter of fact, they come up with new concepts in the law. (R.P. 213.)

Touche Ross unsuccessfully presented the same collateral estoppel issues in motions at and after trial. (C. 10348-58, 11373-416, 11780-82, 11785-86.)

The Congregation sought damages which included the $500,000 invested by the Congregation *after* what the federal courts had found to be disclosure of Newell's losses. (R.P. 3345-46, 3350, 4793.) The jury returned a verdict for the Congregation in the amount of $3.9 million on the negligence claim. (C. 11102.) The trial court entered a final judgment of $3,819,352, representing the entire amount claimed by the Congregation—including the Congregation's final, $500,000 investment. (C. 11682-83.)[8]

Touche Ross asserted the failure of the trial court to afford collateral estoppel effect to the federal determinations as error on appeal (Brief of Touche Ross & Co. filed August 28, 1989 at 33-35; Reply Brief of Touche Ross & Co. filed December 6, 1989 at 11-16), but the Illinois Appellate Court affirmed. The Appellate Court held that the findings of the federal courts were not issue-preclusive because, in the Appellate Court's view, a disposition on motion before trial (here, on summary judgment) did not satisfy the requirements of collateral estoppel and also because, regardless of the specific federal findings, there had been no federal determination on the merits of the Congregation's state law causes of action. (224 Ill. App. 3d at 574; App. B-16-17.)

Touche Ross again raised the failure of the Illinois courts to afford collateral estoppel effect to the federal determinations on

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[8]The jury also returned a $1.5 million verdict on the Congregation's breach of contract count. (C 11103.) However, the Congregation subsequently consented to a remittitur of the award on the contract count to $0. (159 Ill. 2d at 150; App. A-9.)

appeal to the Illinois Supreme Court. (Brief of Appellant Touche Ross & Co. filed May 5, 1992 at 22-23 and 28-39; Reply Brief of Appellant Touche Ross & Co. filed June 30, 1992 at 9-14.) Some two years later, the Illinois Supreme Court affirmed the Appellate Court's judgment in a 4-2 decision. The Court disagreed with the Appellate Court that collateral estoppel was inapplicable to findings made on summary judgment or to federal findings made where state law claims are dismissed for want of pendent jurisdiction. Nonetheless, the Illinois Supreme Court "agree[d] that collateral estoppel does not preclude plaintiff's claim here . . . for reasons different from those advanced by the appellate court." (159 Ill. 2d at 152; App. A-11.)

The Illinois Supreme Court applied Illinois law, rather than federal law, to determine the preclusive effect of the federal determinations. The majority held that under Illinois law, only determinations on issues which are "controlling" in both cases are entitled to preclusive effect. (159 Ill. 2d at 153-54; App. A-12.) Although the federal courts had found, as an independent and sufficient ground for their judgments, that there was "no evidentiary basis" for the allegations of misrepresentation against Touche Ross and that, in fact, Touche Ross had made *no* misrepresentations to plaintiff, the Illinois Supreme Court held that those determinations were not issue-preclusive because the federal courts *could* have ended their opinions after concluding that there had been no primary violation of the securities laws. According to the Illinois Supreme Court, the additional federal determinations relied on by Touche Ross were therefore not "necessary" and were even "irrelevant" *to the federal courts' own judgments*. Specifically, the Illinois Supreme Court held:

> Whether plaintiff agreed with defendant to report Newell's investments at cost in plaintiff's financial reports was not necessary to the Federal adjudication. The Federal security [sic] law claims were based on alleged misrepresentations by Newell and the securities dealers. Defendant [Touche Ross] was accused of aiding and abetting the security [sic] law violations. Once the

> Federal court determined, however, that no misrepresentations were made by the securities dealers to plaintiff, *communications between plaintiff and defendant became irrelevant to the Federal claim.* The Federal courts found that defendant [Touche Ross] could not be guilty of aiding and abetting if no primary violation of the security [sic] laws had been established. *Any agreement between the plaintiff and defendant therefore, was not necessary to the Federal adjudication. For the same reason, any misrepresentations by defendant to plaintiff were not relevant to the Federal claims.* (159 Ill. 2d at 154; App. A-12-13.) (Emphasis supplied.)

The Illinois Supreme Court also held that the federal courts' other findings concerning Newell's agency, the Congregation's knowledge, and its exclusive reliance on Newell were not "relevant" to the Congregation's "theories of recovery" in the *state* case and that therefore they "could have no effect on the judgment in this [state] case." (159 Ill. 2d at 153; App. A-12.) In addition, the Court concluded that it could disregard the federal determination that the Congregation "must now be responsible" for its own losses on the ground that this determination was "taken out of context" and supposedly applied only to the Congregation's dealings with "third parties" other than Touche Ross.[9] (159 Ill. 2d at 156; App. A-14-15.) In dissent, two Justices concluded that the majority had "ignored the federal district court's determinations for collateral estoppel purposes" and that,

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[9]There was another federal determination which the Illinois Supreme Court inexplicably passed over in silence. The Illinois Supreme Court did not mention the finding of the federal courts that the Congregation had given Newell another $500,000 *after* learning of his losses. Instead, without discussing the finding, the Illinois Supreme Court implicitly rejected the preclusive effect of this determination when it said that the question of when plaintiff learned of the losses, in relation to the additional $500,000 investment, *was an issue of fact for the state court jury.* (159 Ill. 2d at 170-71; App. A-27-28.) Thus, the Illinois Supreme Court disregarded the contrary federal finding.

if these findings had been give proper weight, "this case should never have gone to trial." (159 Ill. 2d 183-84; App. A-38-39.)

Touche Ross petitioned the Illinois Supreme Court for rehearing, specifically addressing the Court's failure to give collateral estoppel efffect to the federal determinations. (Petition of Defendant-Appellant Touche Ross & Co. for Rehearing dated May 12, 1994 at 9-15.) The Court denied rehearing on May 27, 1994.

The mandate was returned to the trial court on June 6, 1994, and Touche Ross accordingly was required to pay the judgment. Under Illinois law, payment of the judgment did not impair Touche Ross' right to seek the reversal or vacation of the judgment.[10]

REASONS FOR GRANTING THE WRIT

The Illinois Supreme Court's ruling warrants review by this Court for two reasons, both indispensable to federalism.

First, this case presents significant issues concerning the constitutional obligation of the state courts to honor federal court judgments—and federal law governing the effect of those judgments—by precluding the relitigation of issues previously and

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[10]Section 5/2-1303 of the *Code of Civil Procedure of Illinois*, 735 ILCS 5/2-1303, provides, in part:

> The judgment debtor may by tender of payment of judgment, costs and interest accrued to the date of tender, stop the further accrual of interest on such judgment notwithstanding the prosecution of an appeal, or other steps to reverse, vacate or modify the judgment. (App. G.)

The Illinois Supreme Court has observed that "it is well established that the payment or satisfaction of a money judgment by a judgment debtor does not bar the prosecution of a writ of error or an appeal by such judgment debtor." *Pinkstaff* v. *Pennsylvania R. R. Co.*, 31 Ill. 2d 518, 523, 202 N.E.2d 512, 514 (1964). Similarly, it has long been established in the federal courts that payment of a judgment does not bar an appeal. *Dakota County* v. *Glidden*, 113 U.S. 222, 224 (1885).

finally resolved on the merits by the federal courts. *The key issues in this case were litigated twice, once in the federal system and, over defendant's objection, again in the Illinois courts, and inconsistent results were affirmed by the Illinois Supreme Court.* The federal courts determined that Touche Ross made no misrepresentation to the Congregation concerning the Newell investments, that the Congregation was responsible for the acts of its investment advisor Newell, and that the Congregation "was fully aware of the transactions and the type of risks involved. It must now be responsible for the deficit created when the investments lost money." (800 F.2d at 184; App. E-13.) The state court jury's verdict was the *exact opposite* of the judgment previously rendered in the federal courts.

By applying purported state law principles denying preclusive effect to alternative findings and by limiting preclusive effect only to those findings relevant to the *plaintiff's* theories of recovery (rather than available defenses), the Illinois Supreme Court deprived the prior federal adjudications of any force or effect. If this approach is allowed to stand, it will surely be emulated whenever state courts choose, for whatever reason, to disagree with prior federal adjudications, thus undermining the scope, meaning and finality of federal judgments.[11] *Southwest Airlines Co.* v. *Texas International Airlines*, 546 F.2d 84, 94 (5th Cir.), *cert. denied*, 434 U.S. 832 (1977) ("If state courts could eradicate the force and effect of federal court judgments through supervening interpretations of the state law of *res judicata*, federal courts would not be a reliable forum for the final adjudication of . . . claims.")

Second, the Illinois Supreme Court has decided a federal question—the preclusion effect of alternative federal determinations—"in a way that conflicts with the decision[s]" of several United States courts of appeals. Sup. Ct. R. 10.1(b). The rule in

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[11]Here the dissenting Illinois Supreme Court Justices believed that the majority had been swayed by inappropriate "sympathy" for the Catholic religious order. (159 Ill. 2d at 184; App. A-40.)

most of the circuits which have considered the question is that alternative federal determinations, each an independently sufficient ground for a judgment, are each entitled to collateral estoppel effect; Illinois law, as applied by the Illinois Supreme Court in this case, is directly contrary. One circuit has stated that neither determination is preclusive; this is the view of Illinois law applied by the Illinois Supreme Court in this case. A third, "intermediate" view is that any independent, alternative determination is preclusive if it is expressly reviewed and affirmed on appeal. This Court should resolve the conflict between the Illinois Supreme Court and the majority of the federal courts of appeals, as well as the conflict among the circuits, and hold that all alternative federal determinations are preclusive at least where, as here, they are reviewed and expressly affirmed on appeal.

I. The Failure Of The Illinois Supreme Court To Honor A Federal Court Judgment Gives Rise To A Federal Question Reviewable On Writ Of Certiorari

Article III of the Constitution vests the judicial power of the United States in this Court and "such inferior courts as the Congress may from time to time ordain and establish," and extends that power to "all Cases, in Law and Equity, arising under this Constitution ... [or] ... the Laws of the United States ...." U.S. Const. Art. III, § 1; Art. III, § 2, cl. 1. (App. G.) Implicit in this grant of judicial authority is the assumption that the determinations of the federal courts will be conclusive as to matters within the jurisdiction of those courts. The conclusive resolution of disputes is the very purpose for which courts are established, and the coordinate doctrines of *res judicata* and collateral estoppel are central to that purpose. *Montana* v. *United States*, 440 U.S. 147, 153 (1979). Thus, Article III and the Supremacy and Necessary and Proper Clauses of the Constitution require that state courts give full effect, including collateral estoppel effect, to the judgments and determinations of the federal courts. U.S. Const., Art. I, § 8, cl. 18; Art. VI, cl. 2 (App. G.); *Stoll* v. *Gottlieb*, 305 U.S. 165, 172 (1938). *See also* 1B J. Moore, J. Lucas and T. Currier, *Moore's Federal Practice*

¶ 0.406 [1] at III-82 (2d ed. 1992).[12] As a consequence, the state courts cannot disregard or undertake to review federal court determinations:

> It would be unthinkable to suggest that state courts should be free to disregard the judgment of federal courts given the basic requirement[s] that . . . federal courts must honor state court judgments. The requirement that federal court judgments command at least the central core of *res judicata* effects in state courts is 'indispensable to federalism.' *Williams Natural Gas Co.* v. *City of Oklahoma City*, 890 F.2d 255, 265 n.11 (10th Cir. 1989), *cert. denied*, 497 U.S. 1003 (1990) (citing 18 C. Wright, A. Miller and E. Coopers, *Federal Practice and Procedure* § 4468 at 648-49 (1981)).

This Court long ago recognized that the refusal of a state court to accord preclusive effect to a federal judgment was appealable to this Court as a case "in which a title or right is claimed under an authority exercised under the United States . . . . " *Dupasseur* v. *Rochereau*, 88 U.S. (21 Wall.) 130, 134 (1875). Notwithstanding the importance of the principle that state courts are bound to give effect to federal judgments, a state court's refusal to do so is no longer reviewable by direct appeal to this Court. Moreover, when the collateral estoppel issue has been finally, but wrongly, decided by a state court, injunctive relief is barred by the Anti-Injunction Act. *Parsons Steel, Inc.* v. *First Alabama Bank*, 474 U.S. 518, 525 (1986) (limiting the relitigation exception of the Anti-Injunction Act to cases in which a state court has not yet ruled on the *res judicata* effect of a prior federal adjudication). Thus, where a state court system has finally refused to honor a federal judgment, the *only* available avenue of

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[12]Several decisions of this Court describe the obligation of the state courts to give effect to federal judgments as one of "full faith and credit." *Myers* v. *International Trust Co.*, 263 U.S. 64, 69 (1923); *Deposit Bank* v. *Frankfort*, 191 U.S. 499, 520 (1903); *Hancock Nat'l Bank* v. *Farnum*, 176 U.S. 640, 641-42 (1900).

review to preserve the integrity of the federal adjudicative process is by writ of certiorari.

This Court repeatedly has held that the failure of a state court to honor a federal court judgment gives rise to a federal question reviewable by certiorari. *See, e.g., Stoll, supra*, 305 U.S. at 167; *Toucey* v. *New York Life Ins. Co.*, 314 U.S. 118, 129 (1941). As the Court stated in the course of reviewing a judgment of the Illinois Supreme Court which denied *res judicata* effect to federal court orders:

> Provisions declaring the supremacy of the Constitution and the extent of the judicial power and authorizing necessary and proper legislation to make the grants effective confer jurisdiction upon this Court to determine the effect to be given decrees of a court of the United States in state courts. As the contention is that the ruling below disregarded decrees of a court of the United States, it raised a federal question reviewable under [a predecessor of 28 U.S.C. § 1257(a)]. *Stoll, supra*, 305 U.S. at 167.

The Court's more recent decisions reconfirm that the issue of whether a state court has disregarded a federal court's judicial ruling is reviewable on writ of certiorari. *Limbach* v. *Hooven & Allison Co.*, 466 U.S. 353, 357 (1984) (contention that a state court disregarded a Supreme Court ruling presented an issue reviewable on certiorari); *Parsons Steel, Inc., supra*, 474 U.S. at 525 ("Challenges to the correctness of a state court's determination as to the conclusive effect of a federal judgment must be pursued by way of appeal though the state court system and certiorari from this Court").

In this case, the state trial judge not only failed to give effect to the determinations of the federal courts but also showed overt disdain for the federal courts. The Illinois Supreme Court cast its refusal to honor the federal determinations in more diplomatic terms by invoking state law principles to deny collateral estoppel effect to what it characterized as "unnecessary" and "irrelevant"

federal findings, but the intent and effect of its decision was the same. The Illinois courts deprived the federal judgments of all scope, meaning and finality.

II. The Collateral Estoppel Effect of the Federal Determinations Must Be Measured Against Federal Preclusion Principles

The purpose of the doctrine of collateral estoppel is to preclude the relitigation of matters judicially determined. *Parklane Hosiery Co., Inc.* v. *Shore*, 439 U.S. 322, 326 (1979). In *Parklane,* the Court observed that "[c]ollateral estoppel, like the related doctrine of *res judicata*, has the dual purpose of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial economy by preventing needless litigation." *Id. See also Lytle* v. *Household Mfg., Inc.*, 494 U.S. 545, 553 (1990) (collateral estoppel "protects parties from multiple lawsuits and the possibility of inconsistent decisions, and it conserves judicial resources"). Preclusion principles assume special significance in the context of the federal system where, for political or other reasons, the temptation to second guess or even ignore the judgments of federal courts may sometimes be strong. The preclusive effect of a judgment in a federal question case is governed by federal law. *See, e.g., Limbach, supra*, 466 U.S. at 361; *Stoll, supra*, 305 U.S. at 170-71; *Deposit Bank* v. *Frankfort, supra*, 191 U.S. at 517-20. *See also Gelb* v. *Royal Globe Ins. Co.*, 798 F.2d 38, 41 (2d Cir. 1986), *cert. denied*, 480 U.S. 948 (1987) ("A state court must apply federal law to determine the preclusive effect of a prior federal question judgment"); Restatement (Second) of Judgments, Section 87 (1982) ("Federal law determines the effects under the rules of *res judicata* of a judgment of a federal court"); *Travelers Indemnity Co.* v. *Sarkisian*, 794 F.2d 754, 761, n.8 (2d Cir.), *cert. denied*, 479 U.S. 885 (1986); *Seven Elves, Inc.* v. *Eskenazi*, 704 F.2d 241, 243-44, n.2 (5th Cir. 1983). Thus, the collateral estoppel effect of the federal determinations must be measured against federal preclusion principles.

The Illinois Supreme Court instead applied Illinois law.[13] Illinois law, as articulated and applied in this case by that State's highest court, is contrary to the rule in the vast majority of the federal circuits because it denies collateral estoppel effect to *alternative, independent federal judicial determinations*. Moreover, the Illinois Supreme Court's refusal to afford preclusive effect to federal determinations unless those determinations relate to a *plaintiff's* "theory of recovery" is contrary to basic federal preclusion principles.

III. The Federal Determinations Were Entitled To Preclusive Effect

Under federal law, the doctrine of collateral estoppel precludes the relitigation of an issue determined in prior litigation where: (a) there has been a final judgment on the merits; (b) the party against whom estoppel is asserted is a party or in privity with a party to the prior adjudication; (c) the issue decided in the prior litigation was "necessary" to the decision in that case; and (d) the issue decided in the prior adjudication is identical with one presented in the case in question. *See Parklane Hosiery Co., Inc., supra*, 439 U.S. at 326, n.5; *Montana, supra*, 440 U.S. at 153, 155. Each of these elements is present in this case.

First, it is undisputed that the federal courts rendered a "final judgment on the merits" of the Congregation's securities law claims and on the counterclaims asserted by the broker-dealers against the Congregation. As the Illinois Supreme Court itself recognized, a summary judgment constitutes a final judgment on the merits for collateral estoppel purposes. (159 Ill. 2d. at 152-53; App. A-11-12.) *See also Federated Department Stores, Inc.* v. *Moitie*, 452 U.S. 394, 399 n.3 (1981) (a dismissal of an action for failure to state a claim constitutes a "judgment on the merits" for *res judicata* purposes); *Dicken* v. *Ashcroft*, 972 F.2d 231, 233 n.5 (8th Cir. 1992) ("It is well established that summary judgment is a final judgment on the merits for purposes of *res judicata*").

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[13]The Illinois Supreme Court cited only to Illinois authority. (159 Ill. 2d at 152-54; App. A-11-12.)

Second, the "party" against whom estoppel is asserted, the Congregation, was the plaintiff in the federal court litigation and a counter-defendant on the dealers' counterclaim.

The third and fourth requirements also are met. In the course of adjudicating the Congregation's claims that the broker-dealers and Newell had committed primary violations of the securities laws and granting summary judgment on the broker-dealers' counterclaims, the district court and the Seventh Circuit considered and decided:

(a) that Newell was the Congregation's agent (800 F.2d at 181, 183-84; App. E-8, 12);

(b) that the Congregation vested Newell with full discretionary authority to make investment decisions on its behalf (800 F.2d at 181; App. E-7);

(c) that Newell at all times acted within the scope of the broad discretionary authority conferred upon him by the Congregation (800 F.2d at 184; App. E-13);

(d) that the Congregation relied *only* on Newell and its own advisory board in making investment decisions (800 F.2d at 179; App. E-3-4);

(e) that *none* of the defendants made any misrepresentations to the Congregation (800 F.2d at 182; App. E-8);

(f) that the Congregation was "fully aware of the transactions and the type of risks involved" (800 F.2d at 184; App. E-13); and

(g) that when the Congregation learned of the losses in its account, it entrusted Newell with an additional $500,000 (800 F.2d at 184; App. E-13).

In the course of adjudicating the Congregation's claims that Touche Ross and the broker-dealers had aided and abetted

Newell in violations of the securities laws, the district court and the Seventh Circuit also considered and decided:

> (a) that there was "no factual basis" from which a trier of fact could conclude that Touche Ross or the brokers had aided and abetted Newell by misrepresenting the value of the Newell arbitrage positions (800 F.2d at 183-84; App. E-12); and
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> (b) that Touche Ross and the Congregation had discussed and agreed to the reporting of Newell's arbitrage investments on a cost basis (800 F.2d at 179; App. E-4).

The Seventh Circuit also found that because there was no genuine issue of material fact as to the Congregation's full knowledge of the transactions, the Congregation "must now be responsible for the deficit created when the investments lost money." (800 F.2d at 184; App. E-13.)[14]

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[14]The Illinois Supreme Court chose to construe the Seventh Circuit's determination that the Congregation bore responsibility for its own losses to refer only to the dealings between the Congregation and "third parties," and *not* to Touche Ross, saying that the Seventh Circuit's holding was not intended to adjudicate the Congregation's negligence and breach of contract claims. (159 Ill. 2d at 156; App. A-14-15.) This is both an unreasonably narrow and legally unsound interpretation of what the Seventh Circuit held.

First, it is plainly incorrect to say that the Seventh Circuit intended to exclude Touche Ross from its determination that the Congregation alone was responsible for the losses. The Seventh Circuit's finding was general in scope and related to the entire record before it, including the Congregation's relationship with Touche Ross, the agreement between the Congregation and Touche Ross not to record the Newell investments at market, and the absence of any misrepresentations by Touche Ross. The Seventh Circuit was convinced that the Congregation knew exactly what it was doing and the risks it was taking. (800 F.2d at 184; App. E-13.) Second, the Illinois Supreme Court's observation that the Seventh Circuit did not purport to adjudicate the Congregation's state law claims is wholly inapposite. Of course, the Seventh Circuit was not adjudicating the state law claims; but it *was* making a determination *common* to the federal and state claims.

Each of these findings was necessary to the adjudication of the Congregation's claims and the broker-dealers' counterclaims. Indeed, the Illinois Supreme Court did not question the necessity of most of the federal determinations, nor could it have done so given the fact that all but a few of the findings went directly to the first ground for the federal courts' judgment, i.e., the absence of a primary violation of the securities laws. Instead, the Illinois Supreme court quarreled only with the necessity of the findings that Touche Ross had made no misrepresentations to the Congregation and the related finding that Touche Ross and the Congregation had agreed that the arbitrage investments would be reported at cost. These determinations were independent, alternative holdings supporting the federal judgment and, under the case authority discussed *infra*, at pages 24-27, were equally entitled to preclusive effect.

Finally, each of the issues determined by the federal courts was presented by the Congregation's state law claims. The acts alleged to have constituted "aiding and abetting" Newell were the *very same acts* of "misrepresentation" in Touche Ross' reports of arbitrage values which the Congregation later alleged in the state court. (C. 2-15, 16-41, 11712-28.) Thus, whether there was any "misrepresentation" by Touche Ross in those reports was an identical and critical issue in both actions. If Touche Ross did not "misrepresent" the Newell arbitrage values, the Congregation's state case necessarily would fall.

Moreover, nothing was more "relevant" to the Congregation's state case than its relationship with Newell because the Congregation *had* to prove that Newell lost the funds and how and why he lost them. The nature of the relationship between the Congregation and Newell was alleged in *plaintiff's complaints* in both actions. (C. 2-15, 16-41, 11712-28.) In order to avoid the imputation of Newell's conduct and undoubted knowledge of the market values of the arbitrage positions at all times, the Congregation argued below that Newell was *not* its agent and that the Congregation in any event did not rely on him for knowledge of arbitrage market values. (DX 43; R.P. 1532-33, 1543-44,

2808-09.) However, the agency and reliance issues had already been litigated and lost by the Congregation in the federal courts.[15]

Another key issue was whether the Congregation chose to invest an additional $500,000 with Newell in April 1981—more than two months after the extent of the loss was apparent. The Congregation's causation theory was that if Touche Ross had correctly reported the arbitrage positions, the Congregation would have curtailed Newell's activities. (C. 2-15, 16-41.) But if the Congregation continued engaging in arbitrage investments with Newell *after* learning of his losses, that premise would obviously collapse. It also would mean that Touche Ross could not be responsible for the losses which occurred *after* the Congregation knew the facts. The Illinois Supreme Court held that whether the Congregation learned of Newell's losses before or after it gave him the additional $500,000 *was an issue of fact for the jury.* (159 Ill. 2d at 170-71; App. A-27-28.) The Seventh Circuit, however, had already specifically found that the Congregation entrusted Newell with another $500,000 after "it became

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[15]As the dissent pointed out:

> The majority's finding that none of these issues are relevant to the current theory of recovery is both erroneous and completely conclusory. The plaintiff's theory in this case is that Touche Ross reported the Newell transactions in a negligent fashion, thereby causing plaintiffs losses. As part of this claim, plaintiff must demonstrate that Touche Ross' negligence proximately caused plaintiff's losses. The Federal court finding that plaintiff relied only on Newell and its own business advisory board in making its investment decisions goes directly to the issue of proximate cause. There is no question that Newell and the Board understood the Newell transactions. If the Congregation relied solely on Newell and the Board for the Congregation's investments, how Touche Ross recorded the Newell transactions is irrelevant because Newell and the Board did not base their investment decision on the Touche Ross year-end reports. Had the trial court given proper weight to the Federal Court findings, the case should never have gone to trial. (159 Ill. 2d at 182-83; App. A-38-39.)

apparent that the investments were not good risks" and despite information from Touche Ross that the actual market value of the accounts was $2.4 million less than Newell had reported. (800 F.2d at 180, 184; App. E-4, 13.)[16]

The Illinois Supreme Court excused the trial court's admission of evidence controverting the prior, inconsistent federal determinations on the ground that certain of the federal determinations ostensibly were not relevant to the Congregation's theories of recovery. In so doing, it ignored basic principles governing the collateral estoppel effect of federal determinations.

A. Although There Is A Conflict In The Circuits, The Better Rule Is That Independent, Alternative Grounds For Decision Are Collaterally Preclusive

The federal determinations that Touche Ross did not misrepresent the value of the Newell arbitrage positions and that, to the contrary, Touche Ross and the Congregation had agreed on the accounting treatment for the investments, were "necessary" to the federal adjudication because they were independent, alternative holdings relied upon by the district court in granting summary judgment for Touche Ross. Each of these determinations was expressly discussed and affirmed on appeal by the Seventh Circuit. The rule applied by the Illinois Supreme Court, which denied any effect to the federal courts' holdings because they were reached in the alternative, is contrary to the prevailing view in the federal circuits.

There is a division in the circuits as to whether alternative findings of a federal court, each of which is an independent, ground sufficient to sustain a judgment, are each entitled to

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[16]The majority opinion in the Illinois Supreme Court did not even mention these federal findings which were clearly "relevant"—indeed, dispositive—in the state case *and* "material" to the federal courts' adjudication of the dealers' counterclaim.

collateral estoppel effect. The general rule in the Second,[17] Seventh, Ninth and Eleventh Circuits is that a judgment based on alternative grounds is an effective adjudication as to *both* and is preclusive as to both. *See Ezagui* v. *Dow Chemical Corp.*, 598 F.2d 727, 733 (2d Cir. 1979) (alternative holdings are both grounds for estoppel); *Schellong* v. *U.S. Immigration and Naturalization Service,* 805 F.2d 655, 658 (7th Cir. 1986), *cert. denied,* 481 U.S. 1004, *reh'g denied,* 482 U.S. 921 (1987) ("a judgment which is based on alternative grounds is an effective adjudication as to both and is collaterally conclusive as to both"); *Dewsee* v. *Town of Palm Beach,* 688 F.2d 731, 734 (11th Cir. 1982) ("Normally, each alternative basis would form an independent ground for collateral estoppel"); *In re Westgate-California Corp.*, 642 F.2d 1174, 1176-77 (9th Cir. 1981) (citing the established rule that a judgment concludes each adjudicated issue that is necessary to support any of the grounds upon which a judgment rests). The Fourth Circuit, on the other hand, has stated that a judgment on alternative grounds is not conclusive as to *either* ground, standing alone. *C.B. Marchant Co., Inc.* v. *Eastern Foods, Inc.*, 756 F.2d 317, 319 (4th Cir. 1985) ("the modern rule is that if a judgment rests on independent grounds, either of which would support the result, the judgment is not conclusive with respect to either issue standing alone").

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[17]The Second Circuit has not always followed the majority rule. In *Halpern* v. *Schwartz*, 426 F.2d 102, 106 (2d Cir. 1970), the Second Circuit held that "when a prior judgment adjudicating one a bankrupt rests on two or more independent alternative grounds, it is not conclusive as to issues . . . necessarily found in order to establish only one of those grounds." *Halpern,* however appears to lack any vitality in the Second Circuit, at least outside the bankruptcy context. "Later opinions in the Second Circuit . . . have either suggested that the Halpern rule is a special one that should apply only to bankruptcy cases or have ignored the Halpern opinion entirely." 18 C. Wright, A. Miller and E. Coopers, *Federal Practice and Procedure: Jurisdiction* § 442 at 205 (1981).

The Court of Appeals for the District of Columbia has summarized the criticisms of the two rules as follows:

> A rule declining to accord *res judicata* effect to an alternate ground must of course apply to both grounds, which would mean that a case which is doubly inadequate can be refiled whereas a case inadequate in only one respect cannot. On the other hand, a rule which gives *res judicata* effect to both grounds leaves the losing party who concedes the adequacy of one no appellate remedy for the patent invalidity of the other except a frivolous appeal. *Dozier* v. *Ford Motor Co.*, 702 F.2d 1189, 1194 (D.C. Cir. 1983) (Scalia, J.).

The Restatement (Second) of Judgments § 27 attempts to satisfy these competing concerns by adopting an intermediate ground between those courts which would afford preclusion effect to each of two or more alternative grounds for decision and those which would deny preclusion effect as to all such alternative grounds. Under the Restatement approach, preclusion attaches to every alternative ground of decision which is reviewed and affirmed on appeal, but not otherwise. *Accord, Dozier, supra,* 702 F.2d at 1194 ("since here the losing party did pursue an appeal, which was explicitly rejected *on both grounds*...the dismissal on each ground is *res judicata* in a subsequent suit"); *Hicks* v. *Quaker Oats Co.*, 662 F.2d 1158, 1169-70 (5th Cir.) *reh'g denied,* 668 F.2d 531 (1982) ("we think that the reasoning behind [the Restatement position] is especially appropriate to the facts of this case, where not only do we have an unappealed and allegedly erroneous alternative ground of decision...but plaintiffs seek to use collateral estoppel offensively"). Here, the losing party in the federal litigation sought and obtained appellate review of the district court's decisions, and the Seventh Circuit affirmed on all grounds. Thus, the balance weighs in favor of preclusion. *See* Restatement (Second) of Judgments § 27, Comment o.

Touche Ross submits that the majority rule is best suited to the central purpose of preclusion doctrine—preventing the expense to litigants and the burden on the judicial system which the

unnecessary relitigation of issues entails. As one commentator has observed, "abandonment of estoppel on the mere circumstance that the judgment rests on multiple grounds is not called for and would be totally out of keeping with the developed law in the federal courts that one full and fair opportunity to litigate is enough." 1B J. Moore, J. Lucas & T. Currier, *Moore's Federal Practice* ¶ 0.443[5.-2] at 792-93 (2d ed 1992). Moreover, where, as here, a defendant seeks to employ collateral estoppel defensively, the rationale supporting the minority view is less persuasive. *See Hicks, supra,* 662 F.2d at 1170 ("the arguments against the 'alternative ground' rule are made more persuasive when estoppel is used offensively.")[18]

Under either the majority rule or the Restatement (Second) rule, the federal findings that Touche Ross made no misrepresentations and that Touche Ross and the Congregation had agreed on the accounting method to be employed, were required to be given collateral estoppel effect. These were alternative, independent findings and *all were explicitly affirmed on appeal.* Had the Illinois courts given effect to these determinations, the state court case below would, in the words of the dissent in the Illinois Supreme Court, "never have gone to trial."

B. The Collateral Estoppel Effect Of A Federal Court Judgment Is Not Limited To The Plaintiff's "Theories Of Recovery" In Subsequent State Court Litigation

The Illinois Supreme Court held that several critical determinations of the district court and the Seventh Circuit, though indisputably necessary to the *federal* litigation, were not

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[18]This Court has noted that the *offensive* use of collateral estoppel may actually increase the total amount of litigation and may operate unfairly in some circumstances. *Parklane Hosiery Co., supra,* 439 U.S. at 329-31. As a consequence, the courts have broad discretion in determining whether an offensive use of collateral estoppel should be permitted. *Id.* at 331. No such discretion exists when collateral estoppel is employed in a purely defensive manner, as Touche Ross sought to do here. In this case it is the traditional *defensive* use of collateral estoppel that is at stake.

"relevant" to "*plaintiff's theories* of recovery" in the state court, "could have no effect on the judgment rendered in this [state] case," and thus were not preclusive under *Illinois law*. (159 Ill. 2d at 153; App. A-12.) Among these were the findings: (a) that Newell was the Congregation's agent (800 F.2d at 183-84; App. E-12-13); (b) that Newell had unfettered discretionary authority to invest the Congregation's funds (800 F.2d at 184; App. E-13); (c) that the Congregation relied on Newell, rather than on the other defendants (800 F.2d at 179; App. E-3-4); and (d) that the Congregation was "fully aware of the transactions and the type of risks involved . . . ." (800 F.2d at 184; App. E-13.) The Illinois Supreme Court's holding in this respect is more pernicious—in some respects more insidious—than its outright refusal to accord collateral estoppel effect to the alternative federal findings that Touche Ross made no misrepresentations. A state court desirous of avoiding a prior federal adjudication may always assert, however implausibly, that earlier federal findings were not "relevant" to a litigant's state law "theory." If this process is permitted, it will go far toward undermining the finality of federal adjudications.

Whatever may now be the law of Illinois, the test of collateral estoppel under federal law is not whether the facts adjudicated in one case are relevant only to "plaintiff's theories of recovery" in a later case. The doctrine does not turn on the similarity or identity of the "theories of recovery" in the second case but on the existence of *common issues* where the "theories of recovery" (i.e., causes of action) in the two cases are *different*. *Parklane Hosiery*, *supra*, 439 U.S. at 326 n.5 (contrasting *res judicata*, which "bars a second suit involving the same parties or their privies based on the same cause of action" with collateral estoppel, in which "the second action is upon a different cause of action" but relitigation of "issues actually litigated and necessary to the outcome of the first action" is precluded); *Montana*, *supra*, 440 U.S. at 153 (under the doctrine of collateral estoppel, a determination made in one action "is conclusive in subsequent suits based on a different cause of action involving a party to the prior litigation").

Thus, federal collateral estoppel does not depend on the plaintiff's theory alone but encompasses any issues decided in one action and "relevant" to subsequent litigation, including issues raised by way of defense. In the proceedings below, it was Touche Ross' "theory" that Newell was plaintiff's agent with broad, discretionary investment authority and full knowledge at all times of the *market value* of the arbitrage investments, that plaintiff relied solely on Newell and its own advisory board—not on Touche Ross—for all investment decisions *(including the basic investment decision of whether to allow Newell to continue what the dissent aptly called plaintiff's "big time gambling")*, and that because of his agency both Newell's *knowledge* of the arbitrage market values at all times *and* his negligence were *imputed to his principal, the Congregation*. That is, in fact, the law of agency in Illinois. *Progress Printing Corp.* v. *Jane Byrne Political Committee,* 235 Ill. App. 3d 292, 310, 601 N.E.2d 1055, 1067-68 (1992), *app. denied*, 148 Ill. 2d 653, 610 N.E.2d 1275 (1993); *St. Paul Mercury Ins. Co.* v. *Statistical Tabulating Corp.*, 155 Ill. App. 3d 545, 550-51, 508 N.E.2d 433, 436 (1987); Illinois Law and Practice, Agency § 131.

In any event, the federal findings unquestionably *were* "relevant" to the Congregation's theory of recovery in the state case and they were in fact *relitigated* in the proceedings below. The Illinois trial court's failure to give effect to the federal court findings allowed the Congregation to advance contentions that *directly contradicted* those findings—specifically: (a) that Newell was not the Congregation's agent (*see* R.P. 608, 2645, 2808); (b) that Newell was acting without authority by engaging in arbitrage transactions, by losing the Congregation's invested principal, and by incurring debts to the dealers (*see* R.P. 874-75); (c) that the Congregation relied on Touche Ross in making its investment decisions (*see* R.P. 3648-49, 736-41, 2866-67); (d) that the Congregation's officers were naive clergymen, ignorant of the activity in the Newell account and the nature of his arbitrage transactions (*see* R.P. 643-44, 2819, 2455-57, 1074-75); (e) that the Congregation's officers had not agreed that the market value of the open arbitrage positions would not be

reported in the financial statements (*see* R.P. 1077, 1085, 1697-98; *see also* R.P. 2771-73, 913-14, 1046); and (f) that the Congregation had no responsibility whatsoever for its own losses. (*See* R.P. 2162-63, 2663-65, 4693.) It is utterly facetious to suggest that the issues resolved by the federal courts were irrelevant to the Congregation's theory of recovery in the state court proceeding when the Congregation itself introduced evidence on each of these issues.

CONCLUSION

Petitioner Touche Ross & Co. accordingly requests that a writ of certiorari issue to review the decision of the Illinois Supreme Court and that upon such review, the decision of the Illinois Supreme Court be reversed with instructions that a judgment be entered for Touche Ross & Co. or, in the alternative, with instructions that upon retrial, Touche Ross shall be entitled to an order collaterally estopping the Congregation from denying the matters determined against it in the federal court litigation.

Respectfully submitted,

Francis J. Higgins
(Counsel of Record)
John J. Verscaj
BELL, BOYD & LLOYD
Three First National Plaza
70 West Madison Street
Chicago, Illinois 60602
(312) 372-1121

Attorneys for Petitioner
Touche Ross & Co.

Dated: August 24, 1994

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APPENDIX A

(No. 73224.—Affirmed.)

CONGREGATION OF THE PASSION, HOLY CROSS PROVINCE,

Appellee,

v.

TOUCHE ROSS AND COMPANY,

Appellant.

[Supreme Court of Illinois]

[Reported at 159 Ill. 2d 137 (1994)]

Opinion filed April 21, 1994—Rehearing denied May 27, 1994

JUSTICE MILLER delivered the opinion of the court:

Plaintiff, Congregation of the Passion, Holy Cross Province, brought suit against the defendant, Touche Ross & Company, in the circuit court of Cook County alleging damages resulting from defendant's preparation of financial statements for plaintiff's use. The jury returned verdicts in favor of plaintiff and against defendant for $3.9 million on the negligence count and $1.5 million on the breach of contract count. A directed verdict in favor of defendant had previously been entered on a fiduciary duty count. The trial court entered judgment against defendant for $3,819,352, and the appellate court affirmed. (224 Ill. App. 3d 559.) We allowed defendant's petition for leave to appeal (134 Ill. 2d R. 315), and now affirm the judgment of the appellate court.

Plaintiff is a corporate entity and an order of the Roman Catholic Church. It operates monasteries, retreat houses, and schools. Plaintiff meets its operating expenses by use of contributions and investment income. Rather than make its own investment decisions, plaintiff hires investment advisors to manage its accounts. Defendant is an accounting firm with offices in Chicago and in many other cities throughout the world.

In 1973, plaintiff decided to replace its previous accounting firm with defendant, Touche Ross. Plaintiff and defendant executed an "engagement letter" which listed the services defendant would render for plaintiff. The engagement letter was for a

term of one year. On or about June 30 each year, when plaintiff's fiscal year ended, defendant presented a new engagement letter to plaintiff. In each of the engagement letters, defendant agreed to prepare an unaudited financial statement for plaintiff's use for the fiscal year just ended.

Between defendant's preparation of the 1975 and 1976 fiscal year financial statements, plaintiff appointed Cranford D. Newell of San Franciso, California, as an investment advisor. Plaintiff committed two funds to Newell's control: the "retirement fund" and the "permanent fund." Each fund initially consisted of approximately $1 million. By written agreement, Newell was given full discretionary authority over all investment decisions regarding the two funds.

Newell dealt primarily in government bonds with fixed interest rates. Newell employed a modified "arbitrage" trading strategy. He would buy a bond issue that seemed to be trading lower than government bonds generally, and simultaneously sell short an issue trading higher than securities with similar coupons and maturities. If the market stabilized as Newell anticipated, market forces would move each issue price closer to the prices of other government bonds. The transaction could then be liquidated at a profit. Newell entered into these transactions through accounts held with numerous securities dealers. These transactions were highly leveraged, and although plaintiff had entrusted to Newell only $2 million, Newell held positions on behalf of plaintiff totaling $44.5 million on June 30, 1976. The only cash required by Newell to enter into these transactions was the amount of the purchase less the amount of the short sale. This initial difference between the two amounts is called "margin" or "cost," hereinafter referred to as "cost."

The reports that Newell submitted to plaintiff recorded "open arbitrage positions" at cost. Plaintiff's internal bookkeepers also recorded Newell's arbitrage positions at cost. While the cost figure accurately reflected the market value of an arbitrage position at the moment the transaction took place, any future changes in the market values of the bonds would not be reflected

in the cost figure. Hence, any unrealized losses or gains occurring due to fluctuations in market prices would not be reflected in the cost figures which were reported in the annual financial reports.

Defendant first encountered the Newell investments in the course or preparing plaintiff's 1976 financial statement. The accountants assigned by defendant to prepare plaintiff's 1976 financial statement left in their work papers the following note regarding the Newell investments:

> "3) Arbitrage—when Newell determines that there is a temporary fluctuation in the price of a government security in relationship to other government securities he buys or sells long that security and purchase [*sic*] or sells short another government security at the same time. When the fluctuation is eliminated he reverses his previous purchase and short sale and takes a profit (or loss). These arbitrages are generally for over $1 million dollars [*sic*] and a small fluctuation (1/32 of 1%) can involve a substantial amount of money. The only money actually invested by the Congregation is for margin [cost] required by the dealers (typically the amount of the purchase less the amount of the short sale). The risk is minimized since only U.S. government securities are traded and the chance of default is small.
>
> At June 30, 1976 the Congregation had open arbitrages aggregating $22.25 million at par value and short positions in the same amount. Since the trades in these securities involve minor fluctuations in price (1/32 or even 1/64 of a point) and there is no source which can tell us market value closer than 1 point ($222,500) it was decided not to gross up the balance sheet to reflect these items at market.
>
> Instead footnote disclosure will be made of the total amounts involved and only the margin [cost] outstanding on these arbitrages will be included in investments.
>
> W. Cornfield
> 10/4/76"

During the preparation of the 1976 financial report, the partner of defendant in charge of plaintiff's account, Philip Melchert, called plaintiff's treasurer, Brother James Kent, to inquire about the Newell investments. Plaintiff claims Melchert recommended that the Newell investments be recorded at cost. Melchert purportedly explained that cost was approximately equal to market value. Plaintiff claims that Brother James did not understand the Newell investments and that in agreeing that the investments be recorded at cost, Brother James deferred to defendant's expertise.

Defendant denies that Brother James did not understand the Newell investments. Defendant claims that Melchert and Brother James mutually agreed to report the Newell investments at cost, and that Brother James fully understood the import of that decision.

After defendant completed its work at plaintiff's offices in 1976, Melchert met with plaintiff's governing body, the Provincial Council (the Council), to discuss the annual report. The 1976 financial report contained a footnote which specified that Newell's investments were carried at cost rather than market value. Plaintiff claims Melchert explained this footnote by again stating that cost was essentially equal to market value.

By reporting arbitrage transactions at cost, defendant reported the Newell investments at $2,166,322 in the 1976 financial report. The actual market value of the investments on June 30, 1976, the date of the report, was $1,951,520. By reporting the transactions at cost, there was a discrepancy between the market value of the Newell investments and the figure reported by defendant in plaintiff's financial reports for each fiscal year from

1976-79. The amounts of the discrepancies are shown in the following chart:

Fiscal Year	Figure Reported by Defendant in Report	Actual Market Value at Time of Report	Discrepancy
1976	$2,166,322	$1,951,520	($ 214,802)
1977	1,795,346	1,471,720	(323,626)
1978	1,792,748	878,638	(1,472,887)
1979	2,226,014	319,861	(1,347,376)

Kenneth Witt, an employee of defendant, did the field work for plaintiff's 1980 financial statement. Witt prepared a draft of the 1980 financial statement which defendant sent to plaintiff in September 1980. The 1980 draft reported the Newell accounts at approximately $3.6 million. Because the $3.6 million cost figure did not reflect unrealized losses, the actual market value of Newell's investments was later shown to have been approximately $1.2 million at the time of the report.

Prior to defendant's submitting to plaintiff a final report for 1980, Melchert contacted Witt and asked him where the $3.6 million reported in the draft financial report was located. Witt was unable to answer the question. Melchert then began an independent investigation of the Newell investments and their values. In October 1980, Melchert contacted Newell and requested information regarding plaintiff's funds. Newell was unable to furnish the material that Melchert requested. Melchert next contacted the securities dealers with whom Newell held accounts on plaintiff's behalf. By January 1981, Melchert had received June 30, 1980, market values for the Newell accounts totaling approximately $1.2 million. When Melchert called Newell with this information, Newell informed him that the $1.2 million figure rather than the $3.6 million cost figure reported in the 1980 draft financial report could be the total market value of Newell's accounts with plaintiff.

On February 11, 1981, a week after Melchert spoke with Newell, Melchert attended a meeting of the Council. Plaintiff claims that Melchert informed the Council that the market value

of Newell's accounts was approximately equal to cost; however, recent events had, according to Melchert, caused him to question whether there were unrealized losses. Melchert allegedly offered limited details and promised to investigate the matter further. Defendant contends that Melchert informed the Council he had reason to believe that the market value of the Newell investments was approximately $1.2 million.

Approximately two months after the February 11, 1981, Council meeting, a security dealer made a "margin call" on an account managed by Newell. Newell called plaintiff and requested an additional $500,000 to cover the margin call. Newell explained that if the dealer closed out plaintiff's accounts, substantial "unrealized losses" could be recognized. At the time of the margin call, plaintiff still had in its possession the draft 1980 financial report in which defendant had reported Newell's account at approximately $3.6 million. Plaintiff had not heard anything further from defendant since the February 11, 1981, Council meeting. After a meeting with Newell during which Newell explained the negative consequences of not meeting the margin call, plaintiff's investment officer recommended to plaintiff that the additional $500,000 be forwarded to Newell. On April 14, 1981, plaintiff transferred the additional sum to Newell.

After plaintiff forwarded the additional funds to Newell, plaintiff received from defendant a letter in which defendant stated that the market value of the Newell accounts on June 30, 1978, was $319,860, and not the $1,792,748 cost figure reported in the 1978 financial report. Defendant offered in the letter to discuss the matter further if plaintiff desired.

Late in April 1981, defendant sent plaintiff a copy of the final 1980 financial report. According to the report, the market value of the Newell accounts on June 30, 1980, totaled $1,286,411. "Note H" to the report stated, in part:

> "Since the Congregation carries investments at market value, the amounts reported previously (for the Newell

accounts) have been restated to include unrealized gains and losses as follows:

	Previously Reported	Adjustment	As Restated
June 30, 1978	$1,792,747	$(1,472,887)	$319,860
June 30, 1979	2,226,014	(1,347,376)	876,638"

Shortly after plaintiff received the final 1980 financial statement from defendant, it closed its accounts with Newell. The accounts had not only been substantially depleted, but due to a shift in interest rates, several of the security dealers with whom Newell dealt claimed plaintiff owed them additional sums. After plaintiff settled all claims with the security dealers, plaintiff sustained net losses on the Newell accounts in the amount of $3,819,352.

In addition to testimony regarding the actual conduct of the parties, both defendant and plaintiff presented expert testimony concerning the propriety of defendant's recordation of the Newell investments. Plaintiff's witness, Vincent Sparrow, a certified public accountant and partner of Peat, Marwick & Mitchell, testified that defendant's method of recording Newell's investments violated Generally Accepted Accounting Principles (GAAP). Sparrow further stated that the market values of Newell's investments were readily ascertainable from the Wall Street Journal. Defendant called as a witness Leonard Savoie, the chairman of the department of accountancy and a professor at the University of Notre Dame. Savoie testified that the footnote disclosures contained in the plaintiff's reports were clear in explaining that Newell's investments were not carried at market value. Savoie further testified that this type of footnote disclosure and recordation was in accordance with GAAP.

Prior to filing the complaint here, plaintiff filed a complaint in Federal court against Newell and four securities dealers alleging Federal security law violations. The dealers counterclaimed for amounts due after the liquidation of plaintiff's accounts. In May 1982, plaintiff amended its Federal complaint to join Touche Ross as a defendant, claiming that Touche Ross aided and

abetted the security law violations. Plaintiff also asserted State law claims against Touche Ross. In September 1984, the district court granted the defendants' motion for summary judgment on the security law claims and the aiding and abetting claim. The court declined to exercise pendent jurisdiction over plaintiff's State law claims against Touche Ross, and dismissed those claims without prejudice. Plaintiff appealed the district court's decision, and the Seventh Circuit Court of Appeals affirmed. *Congregation of Passion, Holy Cross Province v. Kidder Peabody & Co.* (7th Cir. 1986), 800 F.2d 177.

After the adverse ruling in Federal district court, plaintiff filed the instant action in the circuit court of Cook County. Plaintiff's complaint consisted of three counts. The first count alleged that defendant was guilty of professional negligence in the manner in which the Newell investments were reported in plaintiff's financial statements. The second count alleged that defendant breached a fiduciary duty it owed to plaintiff by not properly investigating plaintiff's investments and by failing to take appropriate action after it learned of errors contained in the financial statements. The final count alleged that defendant breached its contract with plaintiff by failing to report certain investments in plaintiff's financial statements at market value.

Prior to trial, defendant presented motions to dismiss and for summary judgment. The motions alleged that plaintiff's claims were barred by collateral estoppel because of the findings in the prior Federal litigation, and that the negligence count of plaintiff's complaint was barred by the economic loss doctrine expressed in *Moorman Manufacturing Co. v. National Tank Co.* (1982), 91 Ill. 2d 69. The trial court denied these motions.

After plaintiff presented its evidence and rested its case, defendant moved for a directed verdict on all three counts of plaintiff's complaint. The circuit court denied defendant's motion as to each of the three counts.

At the close of all evidence, defendant renewed its motion for a directed verdict on all three counts of plaintiff's complaint. The

circuit court denied the motion as to the negligence and breach of contract counts, but granted the motion as to the fiduciary duty count.

In its proofs and closing argument, plaintiff sought total damages in the amount of $3,819,352. The jury returned verdicts in favor of plaintiff for $3.9 million on the negligence count and $1.5 million on the breach of contract count. The jury found plaintiff not guilty of any contributory negligence. Because neither the $3.9 million nor the $1.5 million verdict accurately reflected damages sustained by plaintiff, the trial court ordered a remittitur to $3,819,352 on the negligence count and to $0 on the breach of contract count. Plaintiff agreed to the remittitur on the negligence count, but refused to consent to remittitur on the breach on contract count. The trial judge entered what he called a "judgment of liability" on both counts and entered an award of damages in the amount of $3,819,352 on the negligence count only.

The appellate court affirmed the judgment of the trial court on the condition that plaintiff agree to a remittitur of the contract claim to $0. (224 Ill. App. 3d 559.) If plaintiff refused to consent to the remittitur, the case was to be remanded to the trial court on the question of damages. Plaintiff consented to the remittitur. We allowed defendant's petition for leave to appeal to this court. 134 Ill. 2d R. 315.

Defendant alleges here several points of error which it claims are grounds for reversal. First, defendant claims plaintiff was collaterally estopped from contesting issues that were necessary to the result in the parties' prior Federal litigation. Defendant claims that several findings of fact necessary to the result in the Federal litigation were inconsistent with defendant's liability in the present case.

Defendant further claims that the lower court judgment awarding damages for purely economic losses in tort is contrary to *Moorman Manufacturing Co. v. National Tank Co.* (1982), 91 Ill. 2d 69. Defendant further contends that the appellate court

erred in applying the negligent misrepresentation exception to the economic loss doctrine in affirming the trial court.

Finally, defendant claims that the trial court erred in a number of pretrial and evidentiary rulings. Defendant also alleges that because the verdicts did not conform to the evidence, the trial court should have set aside the verdicts.

Plaintiff contends that the judgments below are correct and should be upheld. In the event, however, that this court should determine that further proceedings are required, plaintiff requests the following cross-relief: (1) that the breach of contract verdict be amended to allow full recovery on the contract count; (2) that plaintiff's consent to remittitur on the breach of contract count be rescinded; and (3) that the directed verdict entered in favor of defendant on plaintiff's breach of fiduciary duty count be reversed.

DISCUSSION

I. Collateral Estoppel

In 1981, plaintiff brought suit in Federal district court against its former investment advisor, Cranford D. Newell, and several securities dealers alleging security law violations. Plaintiff later added Touche Ross as a defendant, alleging Touche Ross aided and abetted the security law violations. Plaintiff also alleged State law claims against Touche Ross. Defendants filed a motion for summary judgment, and the Federal district court granted the motion on the security law claims and the aiding and abetting claim. The court, however, declined to exercise pendant jurisdiction over plaintiff's State law claims, and dismissed those claims without prejudice. Plaintiff appealed the district court's grant of summary judgment on the security law claims and the aiding and abetting claim, and the United States Court of Appeals for the Seventh Circuit affirmed. *Congregation of the Passion, Holy Cross Province v. Kidder Peabody & Co.* (7th Cir. 1986), 800 F.2d 177.

Defendant argues that the doctrine of collateral estoppel precludes plaintiff from relitigating those issues decided in the Federal adjudication. Defendant alleges that plaintiff advanced contentions in the present case which directly contradicted the Federal court findings. Plaintiff, on the other hand, claims that those questions decided during the Federal adjudication are not relevant to the present case.

The appellate court believed that because no determination on the merits of the pendent State claims was made by the Federal court, collateral estoppel could not apply. We agree that collateral estoppel does not preclude plaintiff's claims here, but for reasons different from those advanced by the appellate court.

Three factors are necessary for the application of collateral estoppel: (1) the issue decided in the prior adjudication must be identical with the one presented in the case in question; (2) there must have been a final judgment on the merits; and (3) the party against whom the estoppel is asserted must be a party, or in privity with a party, to the prior adjudication. *Ballweg v. City of Springfield* (1986), 114 Ill. 2d 107, 113.

While the Federal court's dismissal of plaintiff's State law claims against defendant was not a final judgment on the merits, collateral estoppel could apply to findings made by the Federal courts while ruling on the security law claims. Plaintiff was a party to the Federal litigation, and there was a final judgment on the merits regarding the security law claims. "Summary judgment *** is the procedural equivalent of a trial and is an adjudication of the claim on the merits." (*Poulos v. Reda* (1987), 165 Ill. App. 3d 793, 801.) Plaintiff, therefore, is precluded from relitigating any findings that were made during the Federal court's adjudication of the security law claims.

Defendant claims that the following findings of fact were made during the Federal adjudication: (1) Newell was plaintiff's agent; (2) Newell had total discretion to act as plaintiff's agent in executing arbitrage transactions; (3) Touche Ross made no misrepresentations to plaintiff; (4) plaintiff was fully aware of the

Newell transactions and the type of risks they involved; (5) Newell acted within his authority; (6) plaintiff relied only on Newell and plaintiff's business advisory board in making investment decisions; (7) plaintiff was able to and did follow the Newell transactions; (8) plaintiff and defendant agreed to report the Newell investments on a cost, not market, basis; and (9) plaintiff was responsible for the losses incurred.

Several of the findings defendant relies on in its collateral estoppel claim are not relevant to plaintiff's theories of recovery here. Accordingly, these findings could have no effect on the judgment rendered in this case. That Newell was plaintiff's agent, that Newell had discretion to invest plaintiff's funds and acted within his authority, that plaintiff was aware of the risks involved in Newell's investments strategy, or that plaintiff relied only on Newell and its own business advisory board in making plaintiff's investment decisions have no bearing on whether defendant is liable to plaintiff for the manner in which defendant recorded the Newell investments in plaintiff's financial report.

We do not believe that the remaining points urged by defendant as findings were actually decided in the Federal adjudication. The doctrine of collateral estoppel applies only to controlling facts or questions material to the determination of both causes. (*Housing Authority v. Young Men's Christian Association* (1984), 101 Ill. 2d 246, 252.) As we explain below, none of the remaining points were necessary to the Federal adjudication, and thus collateral estoppel cannot apply.

Whether plaintiff agreed with defendant to report Newell's investments at cost in plaintiff's financial reports was not necessary to the Federal adjudication. The Federal security law claims were based on alleged misrepresentations by Newell and the securities dealers. Defendant was accused of aiding and abetting the security law violations. Once the Federal court determined, however, that no misrepresentations were made by the securities dealers to plaintiff, communications between plaintiff and defendant became irrelevant to the Federal claim. The Federal courts found that defendant could not be guilty of aiding and abetting if

no primary violation of the security laws had been established. Any agreement between the plaintiff and defendant, therefore, was not necessary to the Federal adjudication. For the same reason, any misrepresentations by defendant to plaintiff were not relevant to the Federal claims.

Defendant further alleges that the Federal courts found plaintiff was able to track the Newell investments. In its opinion, however, the Seventh Circuit stated that plaintiff's ability to track the Newell investments was not necessary to its decision. (*Congregation of the Passion,* 800 F.2d at 182 n.4.) As we have stated, *Housing Authority* holds that collateral estoppel will not attach to this type of finding.

Regarding this point, the dissenting justice asserts that Federal district court found that plaintiff was able to "track" Newell's investments. The quotation contained in the dissent appears in the transcript of the April 30, 1985, hearing at which the district court granted the securities dealers' motions for summary judgment on counterclaims they had brought against the Congregation to collect sums they were owed as a result of Newell's transactions. In opposition to the motions, the Congregation argued that Newell and the dealers had engaged in unauthorized transactions using funds lent by the dealers to Newell. The judge rejected the Congregation's theory, determining that the Congregation was aware of, or could "track," each one of Newell's investments as it was made, that the funds invested by Newell belonged to the Congregation, and that Newell was acting within the scope of his authority in making those investment decisions. With respect to the Congregation's awareness of Newell's activities, the district judge stated at the April 1985 hearing:

> "Simply put, Newell had broad discretion and the plaintiff had knowledge of his activities which it cannot deny. During the years 1975 through 1981, plaintiff was able to track the investments through confirmation slips and accurate reports of the transactions which the dealers supplied. Plaintiff received the statements of its United California Bank account and also had before it those statements, the

> cash sheets and the ticket numbers assigned by Newell for each transaction. The cash transfers were not going into the agent's hands while the principal remained unaware.
>
> In this case, the funds in question were flowing in and out of the plaintiff's own bank account. Therefore, plaintiff was not without knowledge of Newell's transactions during this period of further losses. The documents and the transactions were complex, confusing and ultimately unwise, but the plaintiff had the ability to follow them and to have review of them for themselves or by another specialist other than Newell."

Examination of the district court's entire statement shows that the judge, in speaking of the plaintiff's ability to "track" the investments, was referring only to the plaintiff's knowledge of the particular transactions Newell was entering into on plaintiff's behalf—not that the plaintiff knew the actual extent of Newell's investment losses. As stated earlier in this opinion, both Newell and the securities dealers sent plaintiff confirmation slips accurately detailing all of Newell's transactions. Of course, the confirmation slips showed only the value of the investments when they were made. Future fluctuations in market price were not reported to plaintiff by Newell or the securities dealers. Instead, plaintiff retained defendant to value Newell's investments. The district judge acknowledged that plaintiff could obtain review of Newell's investments by an outside specialist, and it is the asserted negligence of the outside specialist retained for that purpose—defendant, Touche Ross—that is at issue here. In sum, we do not believe that the negligence verdict against defendant in the present case is inconsistent with the statement of the Federal district court regarding plaintiff's ability to "track" Newell's investments.

Finally, defendant points to a statement in the Seventh Circuit opinion that the Congregation must be "responsible for the deficit created when [Newell's] investments lost money." (*Congregation of the Passion,* 800 F.2d at 184.) While this statement may be true when applied to third parties dealing with

plaintiff through Newell, it is clearly taken out of context when applied to plaintiff's relationship with defendant. We do not construe this statement as expressing a view on whether plaintiff could recover from defendant for defendant's independent breach of contract or negligent acts.

We do not believe that any of the issues urged by defendant in support of its collateral estoppel claim are relevant to the present case. The doctrine of collateral estoppel, therefore, does not bar plaintiff's claim here.

II. Economic Loss Doctrine

In count I of its amended complaint, plaintiff alleged defendant owed it a common law duty of due care in the preparation of plaintiff's financial reports. Defendant allegedly breached this duty by reporting the Newell investments at their initial cost rather than at market value at the time of the annual financial reports, and by misstating to plaintiff that the cost of the Newell investments was a reliable indicator of the market value of the investments. In 1978, for example, the Newell investments were reported at their $1,792,747 cost figure rather than their $319,860 market value at the date of the report. Plaintiff claims that defendant's negligence in reporting these values caused it to maintain its accounts with Newell longer than it otherwise would have had it known the market value of the Newell investments. Newell eventually lost $800,000 of the funds he managed for plaintiff, and incurred additional liability of approximately $3 million on plaintiff's behalf.

Count I of plaintiff's amended complaint sought recovery in tort for the depletion of the funds in Newell's control as well as the additional liability incurred by Newell on plaintiff's behalf. Defendant claims that damages alleged by plaintiff in count I of its complaint constitute economic damages and are not recoverable in tort. The issue before us, therefore, is whether the economic loss doctrine bars recovery in tort for accountant malpractice. We find that it does not.

The economic loss doctrine found its roots in *Seely v. White Motor Co.* (1965), 63 Cal. 2d 9, 403 P.2d 145, 45 Cal. Rptr. 17, authored by Justice Traynor. In *Seely*, plaintiff purchased a truck manufactured by defendant. Shortly after the purchase, plaintiff noticed that the truck bounced violently. Despite his efforts, plaintiff was unable to get the problem fixed. Approximately 11 months later, while plaintiff was driving it, the truck overturned. The truck was damaged but plaintiff was not physically injured. After plaintiff repaired the truck, he stopped making payments on the truck. The seller then repossessed the truck, and plaintiff sued defendant on the theories of breach of express warranty and strict liability in tort. Defendant sought damages for the repair of the truck, for money paid on the purchase price and for profits lost by virtue of the truck's unsuitability for normal use. Regarding plaintiff's damages for money paid on the truck's purchase price and for profits lost by virtue of the truck's unsuitability for normal use, the court stated that these economic losses were not recoverable under strict liability in tort. (*Seely*, 63 Cal. 2d at 18, 403 P.2d at 151-52, 45 Cal. Rptr. at 23.) The court explained that products liability grew from the public policy judgment that persons who are injured by dangerous products need more protection than that afforded by the law of warranty. (*Seely*, 63 Cal. 2d at 15, 403 P.2d at 149, 45 Cal. Rptr. at 21.) The *Seely* court believed that if the products liability tort theory were allowed to progress without limitation, however, tort law would wholly engulf contract law. In order to preserve a proper rol[illegible]r the law of warranty and to allow the parties to bargain for the terms of their agreements, the court precluded tort liability in those situations where a defective product caused purely economic losses. (*Seely*, 63 Cal. 2d at 15-16, 403 P.2d at 150, 45 Cal. Rptr. at 22.) The *Seely* court noted that "[t]he distinction that the law has drawn between tort recovery for physical injuries and warranty recovery for economic loss is not arbitrary and does not rest on the 'luck' of one plaintiff in having an accident causing physical injury." (*Seely*, 63 Cal. 2d at 18, 403 P.2d at 151, 45 Cal. Rptr. at 23.) "The distinction rests, rather, on an understanding of the nature of the responsibility a

manufacturer must undertake in distributing his products." *Seely*, 63 Cal. 2d at 18, 403 P.2d at 151, 45 Cal. Rptr. at 23.

This court first addressed the economic loss doctrine in *Moorman Manufacturing Co. v. National Tank Co.* (1982), 91 Ill. 2d 69. In *Moorman*, the plaintiff (Moorman) purchased a grain storage tank from the defendant (National Tank). When a crack developed in the grain storage tank, Moorman sued National Tank for strict liability in tort to recover the cost of repairing the tank and for loss of the tank's use. National Tank argued that Moorman's tort counts were barred because they sought recovery for purely economic loss. The trial court dismissed the tort counts, but the appellate court reversed. In reversing the appellate court and affirming the trial court's dismissal of the tort count, this court noted that the law of sales had been carefully articulated in the Uniform Commercial Code to govern the economic relationship between a seller and buyer. (*Moorman*, 91 Ill. 2d at 78.) The court then stated that application of the rules of warranty to liability prevent a manufacturer from being held liable for damages of unknown and unlimited scope, and that a purchaser is able to allocate the risk of unsatisfactory performance by bargaining for a warranty. (*Moorman*, 91 Ill. 2d at 79.) Accordingly, this court denied Moorman's recovery in tort, stating:

> "Tort theory is appropriately suited for personal injury or property damage resulting from a sudden or dangerous occurrence ***. The remedy for economic loss, loss relating to a purchaser's disappointed expectations due to deterioration, internal breakdown or nonaccidental cause, on the other hand, lies in contract." *Moorman*, 91 Ill. 2d at 86.

In *Moorman*, this court adopted the reasoning of *Seely* that tort law would, if allowed to develop unchecked, eventually envelop contract law. Contract law serves a vital commercial function by providing sellers and buyers with the ability to define the terms of their agreements with certainty prior to a transaction. Where the duty of a seller has traditionally been defined by contract, therefore, *Moorman* dictates that the theory of recovery

should be limited to contract although recovery in tort would be available under traditional tort theories.

This court applied the economic loss doctrine in a real estate context in *Redarowicz v. Ohlendorf* (1982), 92 Ill. 2d 171. In *Redarowicz*, the plaintiff alleged that the defendant was responsible for faulty construction of the plaintiff's residence. The defendant builder completed the house in 1976, and the plaintiff purchased the house from the original owner in 1977. Soon after the purchase, the plaintiff discovered that the chimney and adjoining wall were beginning to pull away from the rest of the house. The court stated that "[a] buyer's desire to enjoy the benefit of his bargain is not an interest that tort law traditionally protects." (*Redarowicz*, 92 Ill. 2d at 177.) The court found *Redarowicz* analogous to *Moorman*, and affirmed the dismissal of the tort count of the plaintiff's complaint. *Redarowicz*, 92 Ill. 2d at 177.

In *Anderson Electric, Inc. v. Ledbetter Erection Corp.* (1986), 115 Ill. 2d 146, this court extended the economic loss doctrine to the furnishing of services. Codefendant Ledbetter retained plaintiff, Anderson, to perform electric work on goods manufactured by codefendant C-E Walther, Inc. Pursuant to a contract between Walther and Ledbetter, Walther was required to inspect and approve Anderson's work. Anderson claimed Walther negligently performed the inspection and approval of Anderson's work, and that as a result of that negligence, Anderson was wrongfully required to redo a substantial amount of work. The court held that Anderson was seeking purely economic damages, and that the economic loss doctrine precluded Anderson's recovery in tort. (*Anderson*, 115 Ill. 2d at 153.) The court reached this result even though Anderson did not have a cause of action in contract. "A plaintiff seeking to recover purely economic losses due to defeated expectations of a commercial bargain cannot recover in tort, regardless of the plaintiff's inability to recover under an action in contract." *Anderson*, 115 Ill. 2d at 153.

A provider of services and his client have an important interest in being able to establish the terms of their relationship

prior to entering into a final agreement. The policy interest supporting the ability to comprehensively define a relationship in a service contract parallels the policy interest supporting the ability to comprehensively define a relationship in a contract for the sale of goods. It is appropriate, therefore, that *Moorman* should apply to the service industry. Just as a seller's duties are defined by his contract with a buyer, the duties of a provider of services may be defined by the contract he enters into with his client. When this is the case, the economic loss doctrine applies to prevent the recovery of purely economic loss in tort.

In *2314 Lincoln Park West Condominium Association v. Mann, Gin, Ebel & Frazier, Ltd.* (1990), 136 Ill. 2d 302, this court employed the economic loss doctrine to deny a client's tort claim against an architecture firm. The plaintiff, Lincoln Park, hired the defendant to design condominium units. Lincoln Park alleged that after the units were completed, the windows and doors were loose, the roof leaked, the garage was settling, and the utilities were inadequate and did not function properly. Lincoln Park brought suit against the defendant on both tort and contract theories. In holding that the economic loss doctrine prohibited Lincoln Park's recovery in tort, this court stated "that the concept of duty is at the heart of distinction drawn by the economic loss rule." (*Lincoln Park*, 136 Ill. 2d at 314.) Because the defendant architect's responsibility originated in its contract, the court found its duties should be measured accordingly. In *dicta*, the court noted that *Lincoln Park* should not be interpreted to stand for the end of all recovery for malpractice in tort. As an example, the court noted that, historically, legal malpractice claims had gone forward in tort because Illinois courts had found that attorneys owe an extracontractual duty which arises not from contract, but from the traditional responsibilities a lawyer owes to a client. *Lincoln Park*, 136 Ill. 2d at 318.

In *Collins v. Reynard* (1992), 154 Ill. 2d 48, this court squarely addressed the issue of whether the economic loss doctrine applies to attorney malpractice. This court held that a complaint against a lawyer for professional malpractice may be

couched in either contract or tort. The concurring opinion stated that an attorney's duty of competence exists "without regard to the terms of any contract of employment entered into by a lawyer and a client." The concurrence went on to explain that "[t]he cases in which *Moorman* has been applied are grounded on the notion that the complaining party, if he wished protection against the particular type of harm suffered, could have bargained for a guarantee or warranty against it." *Collins*, 154 Ill. 2d at 56 (Miller, C.J., specially concurring, joined by Bilandic, Freeman & Cunningham, JJ.).

The evolution of the economic loss doctrine shows that the doctrine is applicable to the service industry only where the duty of the party performing the service is defined by the contract that he executes with his client. Where a duty arises outside of the contract, the economic loss doctrine does not prohibit recovery in tort for the negligent breach of that duty. The present case involves professional malpractice by an accounting firm. The underlying issue is whether the duty an accountant owes to his client is defined by his contractual obligations, or is extracontractual.

While a client contracts with an accountant regarding some general matters, an accountant must make his own decisions regarding many significant matters, and the final decision he makes is not necessarily contingent on the contract he executes with his client. An accountant may offer different levels of service, such as audited or unaudited preparation of financial statements, but within these levels of service, the client is not required or expected to be able to direct the conduct of the accountant through contractual provisions. A client should know that an accountant must make certain decisions independently, and the client had the right to rely on the accountant's knowledge and expertise when those decisions are made by the accountant. This knowledge and expertise cannot be memorialized in contract terms, but is expected independent of the accountant's contractual obligations.

An analogy to the accountant-client relationship can be found in the attorney-client relationship. In both cases, the ultimate result of the relationship between the professional and client is something intangible. Whether the professional produces a legal brief or a financial statement, the value of the services rendered lies in the ideas behind the documents, not in the documents themselves. In contrast to the relationship between an attorney or accountant and their client, the relationship between an architect and his client produces something tangible, such as a plan that results in a structure. The characteristics of a tangible object are readily ascertainable, and they can be memorialized in a contract and studied by the parties. The characteristics of something intangible, however, are much more amorphous than the characteristics of something tangible. It is not necessary or generally possible to memorialize all the elements of "competent representation" in a contract. What is necessary to competently represent a client will normally vary with different situations and cannot be anticipated before performance begins. Further, the law has not traditionally required that these elements be included in the retention contract. Application of the *Moorman* doctrine limiting recovery of purely economic losses to contract, therefore, is inappropriate where a relationship results in something intangible.

"Accountants have long been held to be members of a skilled profession, and liable for their negligent failure to observe reasonable professional competence." (P. Kelly, *An Overview of Accountants' Liability*, 15 Forum 579, 583 (1979).) This duty to observe reasonable professional competence exists independently of any contract. The economic loss doctrine does not bar recovery in tort for the breach of a duty that exists independently of a contract.

Although the question of economic loss was not addressed in *Dail v. Adamson* (1991), 212 Ill. App. 3d 66, the court allowed recovery for accountant malpractice in either tort or contract. (See also *First National Bank v. Brumleve & Dabbs* (1989), 183 Ill. App. 3d 987, 992-93 (tort count for accountant malpractice

held to state a valid cause of action).) Tort law has traditionally afforded an avenue of recovery for accountant malpractice, and *Moorman* does not persuade us to reach a different result in the present case. Further, application of the *Moorman* doctrine supports our conclusion allowing recovery in tort for accountant malpractice.

Plaintiff alleges that defendant committed malpractice by the method it used to record the Newell investments in plaintiff's financial statements. This would be a breach of the extracontractual duty of reasonable professional competence which defendant owed plaintiff. Allowing plaintiff to recover its losses in tort, therefore, is consistent with the economic loss doctrine announced in *Moorman*. In view of this result, we need not consider defendant's additional contention that plaintiff cannot recover under a negligent misrepresentation theory.

III. Other Errors Alleged

Defendant summarily alleges the occurrence of a number of other errors that it believes entitles it to a new trial. We have examined defendant's contentions and fail to find any grounds for reversal.

A. Pretrial Rulings

Prior to trial, plaintiff filed a motion *in limine* attempting to preclude defendant from making any reference to plaintiff's investments other than those investments made by Newell. The trial judge granted the motion over defendant's objection. Defendant contends that plaintiff's other investments show that plaintiff knowingly employed investment advisors who utilized highly speculative investment strategies, and the risk of plaintiff's investment strategy is relevant to whether plaintiff was contributorily negligent in its dealings with Newell. We note that during arguments on the motion *in limine*, defendant contended that plaintiff had a history of retaining investments which were initially unprofitable. Defendant, however, does not pursue that theory here, and we therefore do not address this argument. Plaintiff

asserts that its investment strategy bears no relevance to its claims that defendant negligently valued the Newell investments or that defendant breached its contract with plaintiff.

We agree with plaintiff that the trial court properly allowed the motion *in limine*. Plaintiff's claims relate to the manner in which defendant recorded the Newell investments and not to the risks inherent in those investments. We believe, therefore, that the risks involved in plaintiff's other investments had no relevance to plaintiff's claims.

Defendant next alleges that the circuit court committed reversible error by limiting the scope of *voir dire*. Prior to *voir dire*, defendant proposed that the venire be asked the following questions:

> "(1) Is there anyone here who has made a financial contribution to the Roman Catholic Church or to any order or institution of the Roman Catholic Church including hospitals, monasteries or schools?
>
> (2) Have you or any member of your family ever made a financial contribution to the Passionist Fathers?"

The trial judge rejected these questions. The jurors, however, were asked questions concerning membership in, or employment by, any religiously affiliated institution or organization. Prospective jurors were also asked whether they would give more weight to the testimony of persons who belonged to a religious order. Finally, potential jurors were made aware of the identity of the parties and asked if there was any reason they could not be fair and impartial. The appellate court found no error in the trial court's actions regarding *voir dire*.

In support of the trial judge's ruling, plaintiff contends that the proposed *voir dire* questions were improper because they could have caused potential jurors to reveal their religious affiliation. Plaintiff argues that the other questions asked during *voir dire* were sufficient to disclose the venire's prejudices, and that the

additional inquiry suggested by defendant was not necessary in this case.

Under our Rule 234 (134 Ill. 2d R. 234) the primary responsibility for initiating and conducting the *voir dire* examination lies with the trial judge, and the scope and extent of the inquiry rests within the discretion of the judge. (*Kingston v. Turner* (1987), 115 Ill. 2d 445, 464.) When a proposed *voir dire* question could uncover religious affiliation, therefore, it is within the trial court's discretion whether to allow the question. Generally, when religious affiliation is relevant to potential prejudice, subjects related to religious affiliation are proper subjects of inquiry on *voir dire*. See *Casey v. Roman Catholic Archbishop* (1957), 217 Md. 595, 143 A.2d 627.

We believe, however, that the suggested question regarding contributions to the Catholic Church was too remote from plaintiff's losses to be a proper subject for *voir dire* in this case. Any relationship between a potential juror's contribution to the Catholic Church and plaintiff's losses would be indirect. The trial judge did not abuse his discretion in refusing to ask defendant's first question.

With regard to defendant's second proposed question, concerning contributions to plaintiff itself, defendant argues that a juror might be biased if the juror believed that a portion of the money lost had been contributed to plaintiff by the juror or a member of the juror's family. We agree. Where a juror's contributions to plaintiff could have been included in the funds at issue in the case, the juror's impartiality might be questioned. We believe that the better procedure would have been for the trial judge to ask the venire whether they had made contributions to the Congregation.

We do not believe, however, that the trial judge's refusal to ask potential jurors about contributions to plaintiff denied defendant its right to a trial before a fair and impartial jury. All potential jurors were made aware of the identity of the parties and asked whether they could be fair and impartial. Potential jurors

were also asked whether they were members of, or employed by, any religiously affiliated institution or organization, and whether they would give more weight to the testimony of priests and brothers. Finally, we note that the evidence of defendant's liability was overwhelming. Under these circumstances, we do not believe that the trial judge's failure to ask the second question proposed by defendant warrants reversal.

B. Evidentiary Rulings

During trial, plaintiff was allowed to introduce, over defendant's objection, evidence that Newell had been declared bankrupt. Defendant argues that Newell's bankruptcy had no bearing on the issues involved in the present case and that this evidence was highly prejudicial.

In support of the trial judge's ruling, plaintiff contends that defendant characterized Newell in both the opening statement and closing argument as having caused plaintiff's losses. Plaintiff claims, therefore, that defendant "opened the door" to evidence of Newell's bankruptcy, so that the jury could be told why Newell was not a defendant at trial.

Our review of the record reveals that defendant did not attempt to hold Newell responsible for plaintiff's losses. We do not believe, therefore, that defendant "opened the door" for plaintiff to introduce evidence of Newell's bankruptcy. The circuit court erred in admitting this evidence, which was not relevant to the present case.

We believe, however, that any error in allowing evidence of Newell's bankruptcy was harmless. Plaintiff did not attempt to foster jury bias by portraying defendant as its last possible avenue of recourse. The trial in the present case lasted nearly four weeks, and the trial transcript consumed more than 5,000 pages. The jury was presented with overwhelming evidence on which to find defendant liable. Given the strength of the evidence presented to the jury on the question of defendant's liability, we do not believe that the admission of this evidence denied defendant a fair trial.

Defendant also contends that the trial court improperly allowed the redaction of plaintiff's financial statements to exclude references to investments not made by Newell. Defendant argues that to avoid jury confusion these documents should have been admitted into evidence in their entirety. The appellate court found that the redaction was proper. We agree.

Defendant cites *Beech Aircraft Corp. v. Rainey* (1988), 488 U.S. 153, 172, 102 L. Ed. 2d 445, 465, 109 S. Ct. 439, 451, in which the Court stated "that when one party has made use of a portion of a document, such that misunderstanding or distortion can be averted only through presentation of another portion, the material required for completeness is *ipso facto* relevant." Defendant has made no showing of how redacting the documents could have confused the jury. The admission of evidence is within the sound discretion of the circuit court, and its ruling should not be reversed absent a clear showing of abuse. (*People v. Ward* (1984), 101 Ill. 2d 443.) We find no error in admitting the redacted documents into evidence.

Finally, defendant argues that plaintiff was improperly allowed during trial to characterize defendant as a large international accounting firm with offices throughout the world. Prior to trial, the trial judge denied defendant's motion *in limine* to exclude any reference to defendant's size. Defendant maintains that the only purpose of identifying it in this manner was to suggest to the jury that defendant had ample resources with which to compensate plaintiff for its losses.

Plaintiff argues that the references to defendant's size did not make reference to defendant's wealth. Plaintiff further claims that its relied on defendant's expertise, in part, because of defendant's size and resources, and that defendant's size was relevant to the question of plaintiff's reliance on defendant's advice and financial reports. We agree.

Plaintiff, as part of its case in chief, asserted that it had relied on defendant to give advice regarding the manner in which Newell's investments were recorded. Plaintiff accepted this advice

although its members did not understand the underlying transactions involved. The reasonableness of plaintiff's reliance could have been considered by the jury in determining whether plaintiff was contributorily negligent. Because plaintiff contends that defendant's size and reputation were the basis of its reliance on defendant, the trial court acted properly in allowing reference to evidence related to this issue.

C. Jury Verdicts

Defendant alleges that the jury's verdict of $3.9 million on the tort count of plaintiff's complaint was against the manifest weight of the evidence. Specifically, defendant argues that the evidence clearly shows that it was not responsible for the loss of $500,000 entrusted to Newell in April 1981.

Defendant alleges that plaintiff entrusted an additional $500,000 to Newell after plaintiff was fully informed of Newell's losses. It is not contested that plaintiff entrusted an additional $500,000 to Newell in April 1981. There was conflicting testimony, however, concerning whether plaintiff was fully informed of Newell's losses at that time.

Defendant claims that Melchert informed plaintiff of Newell's losses at a meeting of the Council on February 11, 1981. Plaintiff, however, insists that Melchert provided only limited details to the Council at that time, and that Melchert stated he still believed the "cost" of the Newell investments was approximately equal to their market value. Further, it was established at trial that both the letter containing the correct 1978 market values of the Newell investments and the final 1980 financial report were delivered to plaintiff after it had forwarded the additional $500,000 to Newell.

At what point plaintiff became aware of Newell's losses is a question of fact, the determination of which depended heavily on the credibility of the witnesses. The credibility of witnesses and the weight to be given their testimony are matters for the jury to determine, and unless the jury's determination is manifestly

against the weight of the evidence, its verdict will not be disturbed on appeal. (*Albaugh v. Cooley* (1981), 87 Ill. 2d 241, 249-50.) For the reasons mentioned, we do not believe that the inclusion of the additional $500,000 in plaintiff's award of damages was against the manifest weight of the evidence.

Defendant also contends that the jury verdicts returned on the tort and contract counts of plaintiff's complaint were inconsistent and did not conform to the evidence. The jury returned verdicts in favor of plaintiff for $3.9 million on the tort count and $1.5 million on the breach of contract count. Plaintiff's total damages, however, were only $3,819,352. The trial court ordered remittitur to that amount on the tort count, and $0 on the breach of contract count. Plaintiff consented to remittitur on the tort count, but not on the breach of contract count. The trial court then entered a judgment of liability on both counts, and awarded damages of $3,819,352 on the tort count only. Plaintiff agreed to remittitur to $0 on the breach of contract count in the appellate court as a condition for the appellate court's not remanding the cause for a new trial on the issue of damages.

Defendant contends that the verdicts are irreconcilable and should be set aside. Plaintiff alleges that the jury clearly intended to compensate the Congregation in full for its losses, and that the jury's apparent confusion over awarding damages on each separate count does not warrant reversal.

"[A] verdict must be set aside where the amount of the verdict bears no relationship to the loss suffered by the plaintiff." (*Churchill v. Norfolk & Western Ry. Co.* (1978), 73 Ill. 2d 127, 148.) Verdicts are to be liberally construed, however, and may be amended to conform to the pleadings and evidence contained in the record whenever the intention of the jury is clear. (*Churchill,* 73 Ill. 2d at 148.) Although the $3.9 million verdict returned by the jury on the tort count of the complaint is slightly greater than the amount of the losses suffered by plaintiff, we believe that the relatively minor deviation from plaintiff's actual damages shows that the intent of the jury was to award plaintiff the full amount of its damages on the tort count.

The $1.5 million verdict returned by the jury on the contract count does not bear any ascertainable relationship to the loss suffered by plaintiff. Where plaintiff recovered the full amount of its damages on the tort count, however, the amount of damages awarded on the contract count should not affect its recovery. It is well established that a plaintiff may have only one satisfaction for an injury. (*McLane v. Russell* (1989), 131 Ill. 2d 509, 523.) Both the tort and contract counts were based on the same facts and sought recovery for the same injury. Plaintiff, therefore, could not recover under both counts. Plaintiff acknowledges this limitation on recovery of damages and concedes that $3,819,352 is the maximum amount of its allowable recovery.

Because the jury's intent regarding damages on the tort count of plaintiff's complaint is clear, and damages awarded on the contract count could not affect plaintiff's recovery, we do not believe that the conflicting verdicts warrant reversal of this case.

CONCLUSION

For the reasons given, we affirm the judgment of the appellate court. Accordingly, we need not consider plaintiff's request for cross-relief.

Affirmed.

JUSTICE NICKELS took no part in the consideration or decision of this case.

JUSTICE FREEMAN, specially concurring:

The majority narrowly holds that the economic loss doctrine does not bar a tort claim for accountant malpractice. I agree with the result. The majority reaches this result by concluding that a contract for accountant services, like that for attorney services, has some extracontractual duties, which are not capable of memorialization. The presence of these duties, reasons the majority, distinguishes accountants and attorneys from other professionals, such as architects, where the professional's obligations may be memorialized in the contract. The rule which the majority

here espouses is that "[w]here a duty arises outside of the contract, the economic loss doctrine does not prohibit recovery in tort for the negligent breach of that duty." (Slip op. at 16.) That being the case, an accountant, like an attorney, may be liable in tort for the failure to competently perform his extracontractual duties.

I agree that the extracontractual-duties analysis provides a proper rationale for the holding in this case. This same rationale was offered in the concurring opinion in *Collins v. Reynard* (1992), 154 Ill. 2d 48, 52 (Miller, C.J., concurring), with respect to tort claims for attorney malpractice. I write separately, however, because this rationale appears to me to have broader implications than the majority suggests.

A professional is one with specialized skill and expertise. In any agreement for professional service, there is an unwritten expectation that the professional will perform competently. And, the failure to exercise a reasonable degree of professional care and skill constitutes malpractice. (Slip op. at 18.) These general propositions hold true regardless of the nature of the profession or that a tangible product results from the professional-client relationship. To the extent that extracontractual duties are defined as the expectation of "reasonable professional competence," such duties are present and are implicit in every professional-client contract. Acceptance of the extracontractual-duties rationale clears the way for tort claims in professional malpractice cases in general.

The majority, having concluded that the nature of the recovery here is dictated by the existence of extracontractual duties, is confronted with *2314 Lincoln Park West Condominium Association v. Mann, Gin, Ebel & Frazier, Ltd.* (1990), 136 Ill. 2d 302, an architect malpractice case. In *Lincoln Park*, this court barred the plaintiff's recovery in tort for architectural malpractice, finding that the plaintiff's recovery was confined to contract damages. The majority apparently recognizes that the extracontractual analysis creates an unnatural tension between this case and *Lincoln Park*. To reconcile the two cases, the majority

attempts to distinguish *Lincoln Park*, by adding another layer to the professional malpractice analysis. The majority holds that because something tangible resulted from the architect-client relationship, the plaintiff was only entitled to contract damages.

Because I believe that the architect in *Lincoln Park* owed the client the extracontractual duty to design the structure competently, I disagree that the majority's tangible/intangible distinction makes any difference. Even had no structure resulted from the relationship, the extracontractual expectation of competent performance was present, and under the analysis applied in this case, the plaintiff's cause of action could lie either in tort or contract. In my view, *Lincoln Park* is irreconcilable with this case, and to the extent that its holding is inconsistent with the holding here, it should be expressly overruled.

By failing to simply conclude that architects, like any other professional, owe their clients extracontractual duties, the majority has effectively created the need for a case-by-case determination of which professionals owe such duties. Further, considering that a product resulting from the professional-client relationship may be only incidental to the relationship, the majority's tangible/intangible distinction is tenuous at best. Under the majority's analysis, no matter how incidental the tangible end product is to the service provided, the existence of such a product will serve to bar a tort claim for malpractice. In my view, it is sufficient to say that in the context of a professional malpractice claim, where the duty to perform extracontractual obligations competently has been breached, the professional may be liable in tort.

JUSTICE HEIPLE, dissenting:

I dissent from the majority opinion for three reasons. First, several material issues were decided in the Federal litigation which should have precluded their relitigation in State court. Second, the inconsistent jury verdicts cannot be glossed over. Finally, today's opinion fails to provide guidance in an unnecessarily murky area of law. Once again, this court has plunged into the

quagmire known as the *Moorman* doctrine and dredged up yet another ill-conceived exception to add to the current confusion.

Standing alone, the earlier Federal litigation, giving rise to estoppel, should have resulted in a judgment for the defendant. Even if estoppel were not applied, the defendant deserves a new trial as a result of the inconsistent verdicts. Finally, the majority opinion is incoherent in its discussion of the *Moorman* doctrine. The majority opinion has further muddled rather than clarified *Moorman*.

FACTS

In 1975, plaintiff, the Congregation, created a "retirement fund" for its members initially valued at $1 million. In 1976, the Congregation established a "permanent fund" also valued at $1 million. The purpose of the permanent fund was to provide for the ongoing needs of the religious and lay personnel who assisted the Congregation. Plaintiff's Business Advisory Board (BAB), a lay advisory board of businessmen, accountants, and experienced securities and commodities traders provided investment and general business advice to the plaintiff.

In the course of developing an investment strategy, the Congregation retained Cranford D. Newell Associates (Newell) as its investment manager. By written agreement, the Congregation's retirement and permanent funds were committed to Newell's full discretionary authority.

In order to meet the Congregation's high return expectations of 12% to 15%, Newell engaged in arbitrage transactions in government securities. These arbitrage investments were first made in the 1976 fiscal year.

Arbitrage is the buying of stocks, or in this case, government securities having different maturity dates and interest rates in one market and simultaneously selling them in another market, in order to profit from a price discrepancy. Trades frequently involve more than $1 million and even minor fluctuations (1/32 or 1/64 of a point) can mean large sums of money. It is an investment

strategy that entails great risks. In other words, arbitrage is a fancy name for big time gambling.

Newell's trading strategy was highly leveraged in that the only cash required to establish an arbitrage position was the difference between the amount obtained from the sale and what was needed to pay for the buy. The reports that Newell submitted to the Congregation reflected the open arbitrage positions at what Newell called "margin," in other words, net cash paid, not at the market value of the securities.

The Congregation engaged Touche Ross to perform unaudited reviews of the Congregation's financial statements for the fiscal years 1974 through 1980. The Congregation engaged Touche Ross prior to turning over its funds to Newell, and Touche Ross was not specifically engaged to consult with plaintiff regarding the arbitrage transactions.

Each year through 1979 Touche Ross sent the Congregation an engagement letter, accepted by the plaintiff, which described the anticipated services that Touche Ross would provide to the Congregation. This form of letter was drafted before Newell's arbitrage trading began.

Unbeknown to Touche Ross, there were mounting problems with the arbitrage trading accounts managed by Newell in 1976 and 1977. In the fall of 1980, during the Touche Ross review of plaintiff's June 30, 1980, unaudited financial statements, Philip Melchert, the Touche Ross engagement partner, raised a question concerning the assets supporting the $3.6 million year-end balance which Newell had reported to the Congregation. After numerous requests to the plaintiff and Newell for additional information concerning these accounts, Melchert was finally provided with the information he needed in January 1981. The information Melchert received from Newell and the dealers indicated that the market value of the Newell accounts as of June 30, 1980, was $1.2 million, or $2.4 million less than the investment value reported to the plaintiff by Newell. During a

conference call on February 4, 1981, involving plaintiff's investment officer, Melchert, and James Hart, a trader on the Chicago Board of Options Exchange and a member of the plaintiff's BAB, Newell confirmed that the market value of these accounts at June 30, 1980, was $1.2 million and that the impairment in value appeared to be permanent.

On February 11, 1981, at a Provincial Council meeting, Melchert advised members of the Provincial Council of the information he had obtained concerning the June 30, 1980, market value of the Newell managed accounts. Despite this information, the Congregation took no action to eliminate arbitrage trading, to close the accounts, or to transfer the management of these accounts to someone other than Newell. Instead of liquidating the accounts, on or about April 14, 1981, more than two months after the Congregation had been advised that the value of the Newell managed accounts at June 30, 1980, was $2.4 million less than the investment value reported by Newell, plaintiff decided to invest an additional $500,000 as requested by Newell. Only after the first week in May 1981, when the equity in the Newell accounts had been completely depleted and substantial debts to certain dealers had been incurred, did the plaintiff act to close its accounts.

In June 1981, the Congregation sued its agent, Newell, and four government securities dealers in the United States District Court for the Northern District of Illinois, allegedly Federal securities law violations. The dealers counterclaimed for amounts allegedly owed after liquidation of the Congregation's accounts managed by Newell. In May 1982, plaintiff amended its Federal complaint to join Touche Ross as an additional defendant, charging it with aiding and abetting the dealers and Newell's alleged securities law violations and with breach of fiduciary duty and breach of contract.

In September 1984, the district court granted the defendants' motions for summary judgment, holding that neither Newell nor the dealers had violated the securities laws and that Touche Ross

had not aided and abetted Newell or the dealers. The remaining counts were dismissed for want of Federal jurisdiction.

In rendering its decision, the district court made specific findings that (1) Newell was plaintiff's agent acting within the scope of his authority, (2) the plaintiff was able to "track" and understand the Newell transactions and (3) the plaintiff's "reliance was on Newell." Specifically, Judge Charles P. Kocoras stated:

> "Simply put, Newell had broad discretion and the plaintiff had knowledge of his activities which it cannot deny. During the years 1975 through 1981, plaintiff was able to track the investments through confirmation slips and accurate reports of the transactions which the dealers supplied. Plaintiff received the statements of its United California Bank account and also had before it those statements, the cash sheets and the ticket numbers assigned by Newell for each transaction. The cash transfers were not going into the agent's hands while the principal remained unaware.
>
> * * *
>
> The documents and the transactions were complex, confusing and ultimately unwise, but the plaintiff had the ability to follow them and to have review of them for themselves or by another specialist other than Newell." *Congregation of the Passion, Holy Cross Province v. Kidder Peabody & Co.* (N.D. Ill. April 30, 1985), No. 81-C-3159 (transcript of proceedings).

The Seventh Circuit Court of Appeals affirmed. (*Congregation of the Passion, Holy Cross Province v. Kidder Peabody & Co.* (7th Cir. 1986), 800 F.2d 177, 184.) That court concluded that "[t]he record on summary judgment*** establishes, as a matter of law, that the Congregation authorized and was aware of the type of transactions which created the debts in the accounts maintained with the dealers."

After the adverse ruling in Federal district court, the plaintiff refiled its complaint against Touche Ross in the circuit court of Cook County. The complaint was based upon the same facts and transactions as were the subject of the Congregation's Federal lawsuit.

Plaintiff's complaint consisted of three counts. Count I, a professional malpractice-negligence count, alleged, in essence, that defendant, *inter alia*, negligently "failed to report and described accurately the market value of the Newell investments." Count II alleged that defendant breached its fiduciary duty to the Congregation in "failing to report and describe accurately the market value of the Newell investments." Count III, a breach of contract count, alleged that Touche Ross breached its express and implied contractual obligations to plaintiff by "failing to report and described accurately the market value of the Newell investments." In other words, while there were three legal theories for recovery, the underlying allegations were identical.

Before trial, Touche Ross presented motions to dismiss and for summary judgment which contended that the Congregation's claims were barred by collateral estoppel and that the negligence count was barred by the *Moorman* doctrine. These motions were denied.

After plaintiff presented its evidence and rested its case, defendant moved for a directed verdict on all three counts of plaintiff's complaint. The circuit court denied defendant's motion as to each of the three counts.

At the close of all evidence, defendant renewed its motion for a directed verdict on all three counts of plaintiff's complaint. The circuit court denied the motion as to the negligence (count I) and breach of contract (count III) counts, but granted the motion as to the fiduciary duty count (count II).

In its proof and closing argument, the plaintiff sought total damages of exactly $3,819,352. These damages consisted of $3,293,350.41 in amounts paid to the dealers in satisfaction of their claims against plaintiff and (b) $526,001.59 in other losses.

These damages included the $500,000 invested by the Congregation, after the February 11, 1980, meeting in which Newell's losses were fully disclosed.

The jury returned separate and inconsistent verdicts for plaintiff in the amount of $3.9 million on count I, the negligence count, and $1.5 million on count III, the breach of contract count. The jury reached this result despite the fact that both the tort and the contract counts were based on the same facts and alleged the identical failures on the part of the defendant.

The trial court ordered a remittitur to $3,819,352 on count I and to $0 on count III. The Congregation agreed to the remittitur on count I, but refused to consent to a remittitur on count III. The trial court then entered a "judgment" of liability on both verdicts, ignored the $1.5 million verdict on count III, and entered a "final judgment" in tort alone, of $3,819,352.

The appellate court affirmed the judgment of the trial court on the condition that plaintiff agree to a remittitur of count III, the contract claim to $0.

APPEAL TO THIS COURT

On appeal to this court, defendant argues that the doctrine of collateral estoppel precludes plaintiff from relitigating those issues decided in the Federal adjudication. Defendant claims that the Federal courts fully considered and decided: (1) that Newell was plaintiff's agent; (2) that because Newell had total discretion to act as the Congregation's agent in executing it arbitrage transactions and because plaintiff was aware of each transaction at the time of its execution, the Congregation was liable on the counterclaims of the dealers; (3) that defendants made no misrepresentations to plaintiff; (4) that the plaintiff was fully aware of the transactions and the type of risks involved; (5) that Newell acted within the scope of his authority; (6) that the Congregation relied only on Newell and its own advisory board in making its investment decisions; (7) that the Congregation was able to and did track the Newell arbitrage investments and was aware "as a

matter of law" of the transactions in which Newell was engaged; (8) that the Congregation and Touche Ross agreed to report the arbitrage investments on a cost, not market, basis and Touche Ross included a footnote in the financial statements reflecting that agreement; and (9) that the Congregation itself, rather than Touche Ross or the dealers, was responsible for, and the cause of, the losses incurred. Touche Ross argues that the trial court's failure to give effect to the Federal court findings allowed plaintiff to advance contentions directly contrary to those findings—leading to the adverse judgment.

Without discussion, the majority states that the several findings that Touche Ross relies upon for its collateral estoppel claim are not relevant to plaintiff's theory of recovery. Therefore, these findings could not have affected the judgment rendered in this case. Specifically, the majority finds it inconsequential: (1) that Newell was plaintiff's agent, (2) that Newell had discretion to invest plaintiff's funds and acted within his authority, (3) that plaintiff was aware of the risks involved in Newell's investment strategy, and (4) that plaintiff relied only on Newell and its own business advisory board in making plaintiff's investment decision. 159 Ill. 2d at 153.

The majority's finding that none of these issues are relevant to the current theory of recovery is both erroneous and completely conclusory. The plaintiff's theory in this case is that Touche Ross reported the Newell transactions in a negligent fashion, thereby causing plaintiff's losses. As part of this claim, plaintiff must demonstrate that Touche Ross's negligence proximately caused plaintiff's losses. The Federal court finding that plaintiff relied only on Newell and its own business advisory board in making its investment decisions goes directly to the issue of proximate cause. There is no question that Newell and the Board understood the Newell transactions. If the Congregation relied solely on Newell and the Board for the Congregation's investments, how Touche Ross recorded the Newell transactions is irrelevant because Newell and the Board did not base their investment decision on the Touche Ross year-end reports. Had the trial court given

proper weight to the Federal court findings, this case should never have gone to trial.

The majority further finds that the other issues Touche Ross claims to have been litigated previously were not necessary to the Federal court proceedings, thus collateral estoppel does not apply. In particular, the majority finds that the Federal courts did not need to decide whether or not the Congregation could track the Newell investments. (159 Ill. 2d at 154.) For support of this conclusion, the majority cites a footnote in the Seventh Circuit opinion in which that court stated:

> "While it is not necessary to our decision, we note that there is at least some evidence to indicate that the Congregation could follow the transactions. Sister Flaherty testified that she never made an entry on the ledger unless she was satisfied that confirmation tickets agreed with cash reports from the United California Bank. Dep. Tr. at 169-70. In addition, the Congregation's Business Advisory Board and an outside firm carefully examined Mr. Newell's investments." *Congregation of the Passion, Holy Cross Province,* 800 F.2d at 182 n.4.

The majority, however, fails to mention that the Federal district court specifically determined that "the plaintiff had the ability to follow [the transactions] and to have review of them for themselves or by another specialist other than Newell." That court also determined that the "[i]nvestment decisions were made by plaintiff's investment adviser Newell—in whom [the Congregation] had entrusted full discretion—and were tracked by plaintiff's officers and other advisers." *Congregation of the Passion, Holy Cross Province v. Kidder Peabody & Co.* (N.D. Ill. April 30, 1985), No. 81-C-3159 (transcript of proceedings).

The majority offers no reason why it ignored the Federal district court's determinations for collateral estoppel purposes. The mere fact that the Seventh Circuit found the defendants not liable on a different basis than the Federal district court does not expunge the correctness of the district court's finding. The State

courts should have barred the relitigation of this issue and dismissed plaintiff's case.

THE INCONSISTENT JURY VERDICTS

Apart from the collateral estoppel issues, I am also bewildered at the nonchalance with which the majority has trivialized the confused and inconsistent jury verdicts in this case. While it is understandable that a lay jury may be moved by a sympathetic plaintiff, it troubles me greatly to speculate that a majority of this court may have been similarly swayed.

In count I of its complaint, plaintiff claimed that it was injured and that it sustained damages when Touche Ross negligently failed to, *inter alia*:

> "(a) report and describe accurately the market value of the Newell investments;
>
> (b) promptly advise [the Congregation] of any material change in the nature and/or balance of such investment ***;
>
> (c) physically inspect or confirm by direct correspondence with independent custodians the Newell investments;
>
> (d) test the market value of the Newell investments by reference to published market quotations;
>
> (e) assure accurate Reports on the nature of the Newell investments; ***."

With respect to the contract count, count III, plaintiff incorporated verbatim the same allegations alleged in the negligence count. Under these circumstances, if plaintiff proved its case, the amount of recovery under either theory should have been the same.

Indeed, plaintiff never claimed that its damages would be different dependent on the theory of recovery. Plaintiff claimed the same damages, $3,819,352, for both the negligence malpractice and the contract count.

Nonetheless, the jury managed to return two inconsistent verdicts. The jury awarded plaintiff $3.9 million on the malpractice count, and $1.5 million on the contract count.

These verdicts should have been set aside. It is true that verdicts are to be liberally construed and may be amended to conform to the evidence. (*Churchill v. Norfolk & Western Ry. Co.* (1978), 73 Ill. 2d 127, 148.) In order for a court to amend a jury verdict, however, the intent of the jury must be clear. (*Churchill*, 73 Ill. 2d at 148.) In this case, it is impossible to discern the intent of the jury.

Taken individually, neither verdict is so far removed from the actual loss claimed as to elicit concern. A court could reasonably interpret the $3.9 million malpractice award as the jury's attempt to fully compensate the plaintiff for its entire claim. On the other hand, a court could conclude that the $1.5 million award logically represents the jury's intent to deduct a given amount from plaintiff's claimed losses due to contributory negligence or failure to mitigate damages.

These two verdicts, however, are impossible to justify when taken together. As the majority points out, "[b]oth the tort and contract counts were based on the same facts and sought recovery for the same injury." (Slip op. at 24.) Rather than remanding for a new trial, however, the majority finds that the jury's intent regarding damages on the tort count is clear, thus the conflicting verdicts do not warrant a reversal.

The fatal error in the majority's opinion stems from its individualized and faulty analysis of the verdicts. The majority first finds that the $3.9 million award demonstrates that the "intent of the jury was to award plaintiff the full amount of its damages on the tort count." (Slip op. at 24.) Next, without explanation, the majority finds that the "$1.5 million verdict returned by the jury on the contract count does not bear any ascertainable relationship to the loss suffered by plaintiff." (Slip op. at 24.) This latter finding, however, completely overlooks the

possibility that the jury may have found the plaintiff partly responsible for its losses.

Indeed, the $1.5 million verdict bears no ascertainable relationship to the loss suffered by plaintiff only if the $3.9 million award is viewed as demonstrative of the jury's intent. There is, however, no proof that this is so and the majority does not offer a rationale for its conclusion. It appears that the majority finds that the $3.9 million award bears a true relationship to the amount lost only because it analyzed that verdict first. Had the majority decided to analyze the $1.5 million award first, perhaps it would have found that the $3.9 million award bears no relationship to the loss. In fact, that would make more sense as the plaintiff asked for $3,819,352, not $3.9 million.

Even if we were to ignore the collateral estoppel problem, given the irreconcilable discrepancy in the verdicts arising from the same facts and issues, I would remand this cause for a new trial on that issue alone.

MOORMAN DOCTRINE

Finally, I dissent from the majority's disposition of the *Moorman* doctrine issue. With today's opinion, the majority has infused further confusion into an area of law already inundated with uncertainty. Rather than clearly defining the relationship between professional malpractice and *Moorman*, the majority opinion puts litigants and trial judges in a position of having to guess what the exception of the month is. Yesterday it was attorneys. Today, it is accountants but not architects. Tomorrow, who can say?

At the heart of the economic loss doctrine is the proposition that contract law, and not tort law, provides the appropriate set of rules for the recovery of purely economic damages. As originally defined by this court, economic damages were those "'damages for inadequate value, costs of repair and replacement of the defective product, or consequent loss of profits—without any claim of personal injury or damage to other property.'" (*Moorman*

Manufacturing Co. v. National Tank Co. (1982), 91 Ill. 2d 69, 82, quoting Note, *Economic Loss is Products Liability Jurisprudence*, 66 Colum. L. Rev. 917, 918 (1966).) The rationale for this tort-contract dichotomy originally stemmed from a reluctance of courts to expose manufacturers to open-ended liability for unforeseeable consequential damages. (See generally Way, Note, *The Problem of Economic Damages: Reconceptualizing the Moorman Doctrine*, 1991 U. Ill. L. Rev. 1169.) Thus, in the *Moorman* case, this court denied recovery in negligence for a defective grain storage tank. This court noted that the Uniform Commercial Code specifically allowed sellers to disclaim warranties for qualitative defects and that to allow for the recovery of such defects in tort law would eviscerate the UCC scheme. *Moorman*, 91 Ill. 2d at 79.

While *Moorman* was decided with products liability and the UCC warranty provisions in mind, this court soon extended the reach of the economic loss doctrine to claims for services performed negligently. (*Anderson Electric, Inc. v. Ledbetter Erection Corp.* (1986), 115 Ill. 2d 146.) The subsequent extension of *Moorman* to professional malpractices was then predictable. In *2314 Lincoln Park West Condominium Association v. Mann, Gin, Ebel & Frazier, Ltd.* (1990), 136 Ill. 2d 302, this court took the next step.

In *Lincoln Park*, a condominium association sought damages from the architectural firm of Mann, Gin, Ebel & Frazier. The association alleged that the architects had negligently designed the condominiums that the association's members had purchased from a third party. This court held that the claim was barred under the economic loss rule. This court found that the association's claim concerned the owner's expectation—a difference of quality—and determined that the architect had no duty in tort to protect the unit owners from that type of loss. *Lincoln Park*, 136 Ill. 2d at 317.

Subsequent to *Lincoln Park*, this court was presented with the question of whether the economic loss rule applied to attorneys, thereby barring malpractice suits in tort for purely economic

damages. In *Collins v. Reynard* (1992), 154 Ill. 2d 48, this court created an exception to the general rule and held that a complaint for malpractice may be couched in either contract or tort and that recovery may be sought in the alternative. The opinion, however, stated that this particular ruling was grounded more in historic precedent rather than logic—citing the fact that attorneys have always been sued in tort. The opinion specifically limited the ruling to attorney malpractice cases. *Collins*, 154 Ill. 2d at 52.

The majority now seeks to create a new exception to the economic loss doctrine. While I do not find it overly disturbing that accountants can be sued in tort for purely economic damages, I am concerned by the fact that the majority has adopted a piecemeal approach for determining what services are not protected by *Moorman*.

The majority submits that the doctrine only applies to those service industries where the "duty of the party performing the service is defined by the contract that he executes with his client. Where a duty arises outside of the contract, the economic loss doctrine does not prohibit recovery in tort for the negligent breach of that duty." (Slip op. at 16.) Applied to this case, the majority contends that the "issue is whether the duty an accountant owes to his client is defined by his contractual obligations, or is extracontractual." (Slip op. at 16.) The majority suggests that because an accountant's "knowledge and expertise cannot be memorialized in contract terms, but is expected independent of the accountant's contractual obligations," an accountant can be held liable in tort. Slip op. at 17.

Having concluded that accountants can be held liable in tort, the majority was still left with the impossible task of distinguishing this case from *Lincoln Park*. That is, why does the *Moorman* doctrine prevent recovery in tort for the professional malpractice of architects, but not the professional malpractice of accountants? The majority offers the suggestion that because the relationship between an architect and his client produces something tangible, the duties of an architect, unlike those of an accountant, can be memorialized in contract. The majority further suggests that, in

the case where an intangible product is involved, "[i]t is not necessary or generally possible to memorialize all the elements of 'competent representation' in a contract." (Slip op. at 17.) This purported explanation, however, is not an aid to understanding.

What are these extracontractual duties? If these duties cannot be articulated in a contract, how is it that the client is able to articulate that they have been breached in a complaint. Why is it that a client cannot require, in the contract, that the accountant exercise the knowledge and expertise of the reasonable certified public accountant? Indeed, it appears that in this case, the parties have done just that. The engagement letter from Touche Ross specifically states:

> "We will review the statements of assets and liabilities of the Congregation of the Passion *** and the related statements of support and revenue, expenses, capital additions and changes in fund balances for the years then ended, *in accordance with standards established by the American Institute of Certified Public Accountants.*" (Emphasis added.)

It should be apparent that the parties have anticipated what would be deemed competent representation, prior to performance.

As for the majority's attempt to distinguish architects from accountants, I submit that the majority has set up the proverbial distinction without a difference. Whether the professional/client relationship creates a tangible or an intangible object is completely irrelevant with reference to whether a professional has competently performed his or her duties. Furthermore, to the extent an architect/client relationship can be memorialized with a general catchall clause requiring competent performance, so can an accountant/client relationship. I am not suggesting, however, that the plaintiff in this case should be barred from suing the accountants in tort. On the contrary, I feel that this court should take this opportunity to reevaluate the application of *Moorman* and remove its protection for all types of professional services, rather than engage in a case-by-case determination of whether a

given profession owes some undefinable extracontractual duty to clients or not.

In mapping the future course of the economic loss doctrine, this court should consider the policy behind it. The purpose behind the doctrine, as embodied in *Moorman*, was to protect manufacturers from unforeseen liabilities. To accomplish that result, jurists determined that when a plaintiff's injury consists of disappointed expectations in a product, contract law and not tort law should apply. Unlike contract law, tort law does not ask whether the full extent of the injury was foreseeable, only whether some injury would occur. Thus, a tort remedy for defeated consumer expectations would expose the manufacturer to open-ended liability from all consequences that follow from a given incident. This open-ended liability seems particularly unjust in products cases where the purchasers communicated their needs only to dealers or retailers but not to the manufacturer.

This line of analysis, however, does not pertain to professional services. In the professional/client relationship, the professional is aware, or should be aware, of any potential liability. For example, attorneys should be able to comprehend their client's situation to the extent where they recognize their potential liabilities if they perform their services in a negligent fashion. The same could be said of accountants and architects. Thus, if a client asks an architect to design a building with specific characteristics and the architect negligently fails to do so, the architect should not be able to claim that the damages caused by his or her negligence were unforeseeable.

If one agrees that damages in professional malpractice cases are foreseeable, what theory a plaintiff brings a suit under becomes irrelevant. The extent of damages should be the same in tort or contract. This is borne out in the case *sub judice* where the claimed loss for breach of contract is identical to that for accountant malpractice.

One must also keep in mind that a suit in tort does not mean that a plaintiff suing for purely economic or commercial loss has

automatically won. The plaintiff still has to establish the elements of a tort. That is, the burden of proving duty, breach of duty, causation, and damages remains a prerequisite to recovery.

Indeed, if the economic loss doctrine were ignored for those cases outside the products liability context, the result in those cases leading up to the present state of the law would have been the same. The difference lies only in the fact that this court would not now have to determine whether a defendant owed a plaintiff an extracontractual duty.

For instance, recall that in *Lincoln Park*, a condominium association brought suit against the architects of the condominium. They alleged that the architects had negligently designed the condominiums that the association members had purchased from a third party, Equity Realty. Plaintiffs sought compensatory damages for repairs that the owners were forced to make.

Rather than analyzing this case in terms of the economic loss doctrine, ask whether defendants owed plaintiffs a duty, whether that duty was breached, and whether that breach was the proximate cause of ascertainable damages. In that case, one would have to conclude that the architects did not owe the association members a duty to protect them from these losses. The scope of the architects' duties cannot be interpreted to include disappointed expectation interests of third parties and subsequent buyers.

While this language may sound hauntingly similar to *Moorman*, it is different in a significant manner. This analysis does not bar recovery for economic damages in tort in all cases—only in those cases where the liability is outside the scope of the duty defendant owes plaintiff. Thus, while architects cannot be held liable for the disappointed expectation of subsequent purchasers, they should be held liable for those of their clients.

Had this court taken this path originally, this court would never have had to engage in its incoherent, indeed, impossible task of determining which professionals owe their clients an

extracontractual duty and are thus outside the protection of *Moorman*.

When viewed in this light, there appears to be no reason, other than the improvement extension of the *Moorman* case, to prevent professional malpractice suits for economic damages to go forward in either tort or contract. Extension of *Moorman* into the arena of professional malpractice should be written off as a failed experiment and the economic loss doctrine should be reconfined to cases involving products liability.

For all the foregoing reasons, I respectfully dissent from the majority.

JUSTICE HARRISON joins in this dissent.

APPENDIX B

CONGREGATION OF THE PASSION,
HOLY CROSS PROVINCE,
an Illinois Not-For-Profit Corporation,
Plaintiff-Appellee/
Cross-Plaintiff-Appellant,

v.

TOUCHE ROSS & COMPANY,
Co-partnership,
Defendant-Appellant/
Cross-Defendant-Appellee.

No. 1-89-0922

Appellate Court of Illinois, First District, First Division

December 30, 1991

[Reported at 224 Ill. App 3d 59, 586 N.E.2d 600 (1991)]

Presiding Justice MANNING delivered the opinion of the court:

Following trial, the jury returned a verdict of liability against defendant-appellant/cross defendant-appellee, Touche Ross & Company (hereafter Touche Ross) in favor of plaintiff-appellee/cross plaintiff-appellant, Congregation of the Passion, Holy Cross Province, (hereafter Congregation) on Count I, sounding in accounting malpractice/negligence and assessed monetary damages in the amount of $3,900,000. The jury also returned a verdict of liability against Touche Ross to Congregation on Count III, a breach of contract theory, and assessed damages in the amount of $1,500,000. The circuit court thereafter entered a judgment order: (1) that granted Touche Ross' post-trial motion for an order of remittitur reducing the total judgment from $3,900,000 to $3,819,352; (2) that in all other respects, denied Touch Ross' post-trial motion; (3) that except as expressly provided, denied all post-trial motions of Congregation; (4) that entered judgment on the verdict of the jury on Counts I and III finding Touche Ross liable to Congregation for accounting malpractice/negligence and

for breach of contract, respectively; and (5) that vacated the court's motion for remittitur as to Count III in the amount of $1,500,000 since Congregation filed a statement refusing to consent to the proposed remittitur by the court.

On appeal, this court granted the parties' motions to cite additional authority and submit briefs in excess of the maximum page requirements; thus, the briefs are lengthy and the trial record is voluminous as well. Touche Ross has raised a multitude of issues on review. The alleged assignments of error are:

(1) Whether the circuit court erred in rejecting collateral estoppel arguments with respect to certain findings made by the Federal court in a prior action between the parties?

(2) Whether the circuit court erred in preventing Touche Ross' counsel from asking prospective jurors during *voir dire* about their religious affiliation and financial contributions to the Passionists or Catholic Church?

(3) Whether the circuit court erred: (a) in granting Congregation's motion in *limine* to exclude any reference to Congregation's other investment activities and (b) with respect to other rulings on several motions in *limine*?

(4) Whether the circuit court erred when it denied Touche Ross' motions for summary judgment, directed verdict and judgment notwithstanding the verdict on Congregation's negligence claim by refusing to find, pursuant to the *Moorman* doctrine, that Congregation is precluded from recovering purely economic losses in a tort action?

(5) Whether the circuit court erred when it denied Touche Ross' motions for directed verdict and judgment notwithstanding the verdict on the negligence count where Congregation abandoned its negligent misrepresentation allegations therein during the jury instruction

conference and thereafter amended its complaint to delete all such allegations from the negligence count?

(6) Whether the circuit court improperly denied Touche Ross' motions for directed verdict and judgment notwithstanding the verdict by rejecting its' argument that Congregation knowingly consented to Touche Ross' decision not to report Congregation's investments at their actual value?

(7) Whether the circuit court erred in refusing certain jury instructions proffered by Touche Ross, in particular, an instruction delineating the elements necessary to prove a claim based on negligent misrepresentation, which includes the element of reliance?

(8) Whether the circuit court committed error when it denied Touche Ross' motion for a new trial agreeing with the jury's finding that Congregation was 0% contributorily negligent?

(9) Whether the circuit court erred in denying Touche Ross' motion for a new trial when Congregation refused to consent to the court's remittitur of damages order?

CROSS-APPEAL

(10) Whether the circuit court erred in denying Congregation's claim for prejudgment interest?

(11) Whether the circuit court erred in directing a verdict against Congregation at the close of all of the evidence on its' claim for breach of fiduciary duty?

(12) Whether the jury's award of $1.5 million to Congregation on the breach of contract claim should be increased to $3,819,352, the amount stated and requested by Congregation as damages sustained?

BACKGROUND

The following facts are set forth from the record below. Touche Ross is an accounting firm that was organized as a co-partnership. Congregation is a Roman Catholic religious community consisting primarily of priests and brothers. It is organized as a not-for-profit corporation and serves as one of two provinces in the United States. Congregation maintains headquarters in Chicago, Illinois and operates monasteries, retreat houses and schools in roughly the western two-thirds of the United States. Religious work is funded by outside contributions and income from capital the governing body (hereinafter the Provincial Council) has invested over the years.

Congregation hired investment specialists and advisors to manage its funds and portfolios. Prior to 1972 a Chicago-based accounting firm prepared the annual financial statements which included reports on the portfolios. In 1973 Congregation engaged the Chicago office of Touche Ross to perform and prepare a review of Congregation's financial statement for the year ending June 30, 1973. Beginning in 1973 and continuing each year through June 30, 1980, Touche Ross and Congregation entered into an agreement known as the "engagement letter" which delineated the services Touche Ross was to provide to Congregation. The engagement letter included a provision that Touche Ross was to "prepare unaudited financial statements for your use (Congregation's use) for the year ended June 30, 19__." The letter also stated that "[w]e wish to emphasize that our engagement is not for the purpose of expressing an opinion on the financial statements and accordingly, the unaudited statements which we prepare will not satisfy any regulatory, contractual, or other requirements for an audit in accordance with generally accepted auditing standards. Furthermore, our engagement is not designed to disclose defalcations or other similar irregularities." The engagement letter provided Congregation with the responsibility "for the proper recording of transactions in the books of account*** and for the substantial accuracy of the financial statements."

With respect to the provision regarding investments, which primarily is the subject of this appeal, the engagement letter provided, in part:

> Investments. Investment securities are to be physically inspected or confirmed by direct correspondence with independent custodians. Investment market values will be tested by reference to published market quotations. Interest due and dividends declared on investments held during the year will be agreed to reported receipts."

In July 1975 Congregation and Cranford Newell, an investment advisor, entered into an agreement authorizing Newell to manage certain funds for Congregation and granting Newell "full discretion" to manage the "Retirement Fund," which had an initial value of approximately $1,000,000. In early 1976 Congregation also established a "Permanent Fund" and committed an additional $1,000,000 to Newell's management.

In 1976 Touche Ross began reviewing the new portfolio managed by Newell. The engagement partner, Phillip R. Melchert (hereinafter Melchert), who was responsible for Congregation's reports from 1974 onward, designated a manager and one or two junior employees who actually went through the accounts at Congregation's offices and prepared the workpaper notes and drafts. In 1976 one of the juniors assigned to Congregation's investment review was William Cornfield (hereinafter Cornfield) and the manager was Duane Oesterreich (hereinafter Oesterreich). In the year-end reviews, Touche Ross accountants worked closely with Brother James Kent (hereinafter Bro. Kent), Congregation's internal accountant and bookkeeper, and after Bro. Kent left the province, they worked with Sister Jeanette Flaherty (hereinafter Sr. Flaherty), Congregation's assistant treasurer/bookkeeper.

The Newell investment activity primarily involved "arbitrage"[1] transactions in "Governments,"[2] but also included some securities or bonds issued by corporations or municipalities. Newell's trading strategy involved highly leveraged arbitrage positions in Governments and he established and maintained accounts with 10 or more government securities dealers, including Kidder Peabody & Co., The First Boston Corp., Bankers Trust Co., and Briggs, Schaedle & Co. Every dealer through whom Newell made a transaction; *i.e.*, opened, closed or repriced a position, sent confirmations relating to the transaction to Newell and directly to Congregation. It is not disputed that Newell also regularly sent a confirmation to Congregation which identified the securities purchased or sold, coupon value, face value, market value, accrued interest on the bond or note, if any, and other information.

According to the parties' briefs on appeal, problems commenced with the Newell reports when the question arose concerning the manner in which the Newell open arbitrage positions would be reported in Congregation's financial statements for the fiscal year ended June 30, 1976. According to Touche Ross' version of the facts, Bro. Kent advised them that he was having difficulty in determining the value of the arbitrage positions and that he was not recording the market value of these open positions on the internal records of Congregation. According to Congregation, Cornfield spoke to Bro. Kent and asked for an explanation of the transactions in the Governments' positions. When Newell began the arbitrage, Bro. Kent commenced recordation of the information received on the Newell confirmations on Congregation's spread sheets. The spread sheets included one figure which

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[1]The Dictionary defines "arbitrage" as the purchase of securities on one market for immediate resale on another in order to profit from a price discrepancy.

[2]"Governments" are bonds issued by the Treasury or by federal agencies.

Newell denoted as "margin."[3] In any event, Cornfield and Oesttereich met with Father Parsons, Congregation's treasurer, and Bro. Kent to determine how to reflect the Newell open arbitrage positions in Congregation's financial statements.

Allegedly, Cornfield and Oesterreich told Congregation that they would discuss the matter with senior management at Touche Ross and come back with a recommendation. The two accountants prepared a workpaper note, which was uncovered during discovery proceedings, but never delivered or shown to Bro. Kent or anyone else at Congregation. The note states:

> "3) Arbitrage-when Newell determines that there is a temporary fluctuation in the price of a government security in relationship to other government securities he buys or sells short that security and purchase [sic] or sells short another government security at the same time. When the fluctuation is eliminated he reverses his previous purchase and short sale and takes a profit (or loss). These arbitrages are generally for over $1 million dollars [sic] and a small fluctuation (1/32 of 1%) can involve a substantial amount of money. The only money actually invested by the Congregation is for margin required by the dealers (typically the amount of the purchase less the amount of the short sale). The risk is minimized since only U.S. government securities are traded and the chance of default is small.
>
> At June 30, 1976 the Congregation had open arbitrages aggregating $22.5 million at par value and short positions

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[3]"Margin" is defined as the difference between the cost and the selling price of securities or commodities, *i.e.*, net cash paid.

"Market value" is defined as the amount that a seller may expect to obtain for merchandise, services, or securities in the open market.

The briefs also reflect that all Governments trade every day through hundreds of dealers. The market prices of this over-the-counter trading are reported daily in the *Wall Street Journal*, as well as other publications. Bonds and notes are quoted in market values of 1/32nds of a point (*e.g.*, "Bid 97-24, Ask 97-28" means dealers stand ready to buy that issue at 97 24/32% of par and will sell it at 97 28/32% of par, par value is always $1,000.)

in the same amount. Since the trades in these securities involve minor fluctuations in price (1/32 or even 1/64 of a point) and there is no source which can tell us market value closer than 1 point ($222,500) it was decided not to gross up the balance sheet to reflect these items at market.

Instead footnote disclosure will be made of the total amounts involved and only the margin outstanding on these arbitrages will be included in investments.

W. Cornfield
10/4/76"

Thereafter, ostensibly following a discussion of the matter with Touche Ross, Bro. Kent and Sr. Flaherty, recorded and reported the Newell open arbitrage positions in Congregation's internal financial records at "margin" or net cash. Touche Ross reported the arbitrage investments on a cost basis and the resulting accounting method made Newell's investments appear profitable. Congregation asserts that this "decision" made by Touche Ross in the form of a recommendation to report the Newell investments in this manner formulates the essence of Touche Ross' negligence. Touche Ross contends that the "decision" was an agreement between it and Father Parsons determining that the market value of the Newell open arbitrage positions *would not* be reported in Congregation's financial statements; furthermore, Congregation did not provide it with any investment market values in 1976 or thereafter for those positions. Additionally, the figure that went into Touche Ross' annual report was the net margin as recorded in Congregation's records.

In the proceedings below and on appeal, it is Congregation's contention that any agreement or decision on how to report the open arbitrage positions did not relieve Touche Ross of any of the obligations that were set forth in the engagement letters in general, and in particular, as set forth in the "investments" paragraph therein. Congregation argues that Touche Ross was negligent for failure to inspect or confirm the securities or "test"

the investment market values to published market quotations. On the other hand and conceding no liability, Touche Ross urges that Congregation knew of the realized losses in Newell's accounts because of several occurrences that transpired beginning in 1976, but did nothing to terminate Newell's contract, restrict his authority or warn Touche Ross.

Each year after 1976, Congregation maintained spread sheets which detailed the Newell information and then provided this information and a schedule based on the sheets to Touche Ross, who in turn totalled up the margins and reported that figure as "investments." The Touche Ross report for the fiscal year ended June 30, 1976 (and for fiscal years 1977, 1978 and 1979 thereafter) (hereinafter annual report) consisted of two sections: (1) the unaudited financial statements of Congregation that were reviewed by Touche Ross and (2) additional information. The Newell open arbitrage positions were included in the summary of investment activity schedule within the additional information section of the annual report. The conventional Newell investments were included at market value, while the open arbitrage positions were included at "margin." Touche Ross added a footnote to the financial statements, which was included in each annual report and disclosed that the open arbitrage positions were not reported at market value.

After Touche Ross completed work at Congregation's offices in 1976 and in subsequent years, Melchert met with members of the Provincial Council to discuss and review the contents of the annual report. The following chart shows the Newell activity as reported by Touche Ross in comparison with the actual market value:

Fiscal Year	Value Reported By Touche Ross	Actual Market Value	Unreported Losses on Financial Stmts. Prepared by Touche Ross
1976	2,166,322	1,951,520	214,802
1977	1,795,346	1,471,720	323,626
1978	1,792,748	319,861	1,472,887
1979	2,226,014	878,638	1,347,376
1980 Draft	3,706,190	1,286,410	2,419,780

According to Congregation, Touche Ross advised them that the Newell reports were substantially accurate; however, they misstated the actual market value of the open arbitrage positions from 1976 to 1980. Congregation alleges that after Mr. Witt, a Touche Ross employee who completed the 1980 field work, showed the value of Newell managed investments to be worth $3,700,000, Melchert came to Congregation's offices to conduct an investigation of his own. During the investigation, Melchert initiated his first contact with Newell in which he discussed the arbitrage situation. Subsequently, Melchert placed a conference call to the salesman for Kidder Peabody, the dealer with the largest Congregation positions, and learned that the market value of the securities in Kidder's custodianship as of June 10, 1980, had been just over $225,000. Melchert then informed Congregation that he was having problems with gathering information on the Newell investments; however, the final 1980 annual report was forthcoming.

Touche Ross asserts that Melchert raised a question concerning the assets in support of the $3.6 million year-end balance which Newell reported to Congregation and after numerous requests to both Congregation and Newell for additional information, Melchert was finally provided with the information he needed in January 1981. The information revealed that the market value of the Newell accounts as of June 30, 1980 was $1.2 million, or $2.4 million less than the investment value reported to Congregation by Newell. The information was confirmed in a conference call on February 4, 1981, which included Brother Kevin O'Malley (hereinafter Bro. O'Malley), who became Congregation's investment officer in late 1976 when Father Parsons divided the responsibilities of treasurer into two positions—the existing position of treasurer and the new position of investment officer; Melchert; and James Hart, a trader on the Chicago Board of Options Exchange and member of Congregation's Business Advisory Board (hereinafter BAB).

Following several meetings and conferences with members of the Provincial Council, BAB and Touche Ross to discuss the

arbitrage situation, during which time the equity in the Newell accounts had been depleted and substantial debts to certain dealers incurred, Congregation closed all Newell open position accounts with the four dealers. The dealers then made claims for account deficits aggregating more than $3,200,000.

THE FEDERAL LITIGATION

In June 1981 Congregation sued Newell and several government securities dealers alleging Federal securities law violations. The dealers counterclaimed for amounts owed by Congregation after liquidation of the accounts. In May 1982 Congregation amended the Federal complaint to join Touche Ross as an additional defendant, and charged them with aiding and abetting the dealers' and Newell's securities law violations, breach of fiduciary duty and breach of contract. Following extensive discovery, in September 1984 the district court granted defendants' motions for summary judgement, finding that neither Newell nor the dealers had violated the securities law and that Touche Ross had not aided and abetted non-existent securities law violations. The Federal court then dismissed the pendent common law State claims against Touche Ross for want of jurisdiction. *Congregation of the Passion, Holy Cross Province v. Kidder Peabody & Co.* (7th Cir. 1986), 800 F.2d 177, 179, 183-84.

CIRCUIT COURT PROCEEDINGS

In 1984 Congregation filed a lawsuit against Touche Ross in the circuit court of Cook County that was comprised of three counts: professional malpractice/negligence, breach of fiduciary duty and breach of contract. The professional malpractice/negligence (hereinafter negligence) count alleged, *inter alia*, that the annual reports negligently reported the Newell investments on a basis other than market value, thus misleading Congregation by failing to disclose unrealized losses; that Touche Ross made negligent misrepresentations and omissions in its reports in the Review of Financial Statements; and that Touche Ross made other oral and written misrepresentations.

Prior to trial, Touche Ross presented motions to dismiss the complaint and for summary judgment, contending that Congregation's overall claims were barred by collateral Estoppel and that the negligence count was barred by the *Moorman* doctrine. the circuit court denied the motions; however, before the jury was selected the circuit court disposed of several motions in *limine* that were filed by both parties. The rulings included orders: that allowed Congregation to introduce evidence concerning Newell's bankruptcy and that Touche Ross was a large accounting firm with offices throughout the world; that foreclosed Touche Ross from presenting evidence about Congregation's other investments, from alluding in any way to the Federal court proceedings or in arguing the collateral estoppel effect of the Federal court findings.

Prior to *voir dire*, Touche Ross' counsel requested leave to ask the prospective jurors questions about their religious affiliation and financial contributions to the Passionists or the Catholic Church. However, the circuit court denied the request and severely restricted questions on the subject of religion.

At the close of all the evidence, during the conference on jury instructions, Touche Ross proffered an instruction concerning the elements necessary to prove a negligent misrepresentation claim. Touche Ross contends that when it proffered the instruction to the circuit court, Congregation's counsel replied that it was no longer alleging a claim based on negligent misrepresentation and then amended the complaint to delete all allegations of misrepresentation from the negligence count. The circuit court then refused Touche Ross' instruction and gave the jury an IPI negligence instruction that did not require the plaintiff to prove the making of any misrepresentation or justifiable reliance. The circuit court instructed the jury separately on the negligence and contract counts and also directed a verdict against Congregation on its breach of fiduciary duty claim.

Congregation claimed compensatory damages for losses sustained after December 31, 1976, and its expert determined that there had been a net loss of funds invested with Newell of $1,439,574. The dealers' claims amounted to $3,293,350, for a

subtotal of $4,732,924 lost or paid out. It was discovered that at some point full payment had been made on a single purchase involving $1,700,000 face amount of a long term bond issue held in the custody of Bankers Trust. When these bonds were sold, Bankers Trust deducted the deficit amount it was owed, and there remained $913,572 which was returned to Congregation. Thus, after subtracting the cash recovery from Banker's Trust, Congregation claimed compensatory damages in the amount of $3,819,352.

The jury returned separate verdicts for Congregation in the amount of $3.9 million on the negligence count and $1.5 million on the breach of contract count. On the negligence count, the jury found Congregation to be 0% contributorily negligent. When the circuit court instructed the clerk to enter judgment on the verdict, the clerk added the two amounts and recorded a judgment of $5.4 million. Following lengthy post-trial proceedings the circuit court denied Touche Ross' motions for judgment notwithstanding the judgment and for a new trial and ordered remittitur to $0 on the breach of contract count and to $3,819,352 on the negligence count. Congregation agreed to remittitur on the negligence count, but refused consent to remittitur on the breach of contract count. The circuit court then entered a judgment of liability on both verdicts and a final judgment of $3,819,352.

As a threshold matter, Touche Ross contends that because the final monetary judgment was in the exact amount of the negligence verdict, as reduced by Congregation's consent to the remittitur, it appears as if the circuit court entered judgment on the breach of contract verdict on liability only. Although the jury assessed damages in the amount of $1.5 million on the breach of contract claim, yet no monetary judgment for breach of contract exists, Touche Ross argues that the scope of this appeal should be limited to negligence issues only.

Touche Ross has not cited any authority in support of this proposition. The record reflects that Congregation's complaint asserted allegations of fact based upon three theories of recovery. The circuit court directed a verdict against it on the breach of

fiduciary claim, and gave instructions to the jury on the remaining two claims sounding in negligence and breach of contract. The jury found Touche Ross liable on both of the remaining theories since it returned separate verdicts and damage award amounts on the respective counts. However, the circuit court was required to enter an order of remittitur as a plaintiff is entitled only to recover actual losses, absent allegations and proof of additional damages, *i.e.*, punitive or special damages. Here, Congregation alleged actual damages in the amount of approximately $3.9 million dollars and as a result it was not entitled to receive the purported combined jury award of $5.4 million. Accordingly, we agree with Touche Ross that because of the inconsistent verdicts; *i.e.*, $3.9 million on the negligence verdict and $1.5 million on the breach of contract verdict, it is incumbent upon this court to review the issues presented by both the negligence and breach of contract claims, as well as address the question of whether the assessed damage awards reflects confusion, prejudice or inconsistency on the part of the jury.

I. Collateral Estoppel

Touche Ross asserts that the circuit court erroneously refused to give collateral estoppel effect to findings of the Federal courts made in a prior action involving the parties here and security dealers and that such errors allowed Congregation to advance contentions in the circuit court which were contradictory to and "necessarily inconsistent" with findings of fact made on identical issues by the Federal courts. (*Wozniak v. County of DuPage* (7th Cir. 1988), 845 F.2d 677, 682-83; *Buttitta v. Newell* (1988), 176 Ill. App. 3d 880, 882-84, 531 N.E.2d 957, 959-60.) They contend that in the Federal litigation, the district court and the court of appeals determined that Newell was Congregation's agent; Newell acted within the scope of his authority; Congregation relied on Newell and BAB in making its investments decisions; Congregation was able to track the investments; Congregation and Touche Ross agreed to report the investments on a cost basis; and Congregation itself, was responsible for, and the proximate cause of, the losses incurred. Thus, the Federal

courts concluded that: (1) the dealers did not commit primary violations of the Federal securities laws; (2) Newell did not commit a primary violation of the Federal securities laws; (3) Congregation was liable on the counterclaims of the dealers since Newell had discretion to act as its agent in executing the arbitrage transactions and Congregation was aware of each transaction; and (4) Congregation was responsible for the deficits created when the investments lost money since it was fully aware of the transactions and the type of risks involved.

In support of its argument, Touche Ross refers to the case of *Buttitta*, where this court held that the findings made in a prior action barred the plaintiff from later establishing that the defendant's negligence caused his losses. In the first action, plaintiff was found to have knowingly violated the Interest Act. Plaintiff then sued defendant, his attorney, alleging negligent advisement; however, the court determined that the earlier finding barred the plaintiff's claim alleging defendant's negligence as the cause of damages incurred. (*Buttitta*, 176 Ill. App. 3d at 884, 531 N.E.2d 957). Thus, Touche Ross contends that the findings of the Federal courts, if given Collateral Estoppel effect, preclude Congregation from arguing that Touche Ross' alleged negligence and breach of contract caused the investment losses since the Federal courts determined that Congregation and its own agent were the cause of the losses incurred.

Congregation contends that Touche Ross' collateral estoppel arguments were correctly rejected at different stages in the proceedings before the circuit court by three different judges, all of whom determined that the issues relevant to the instant action were never fully and fairly litigated in the prior Federal case. Specifically, Congregation urges that the decision in the Federal case was limited to the securities fraud action against the dealers with whom Newell made the investments in Governments, rather than Congregation's pendant State law claims against Touche Ross.

Collateral estoppel (issue preclusion) applies when a party "takes part in two separate, consecutive cases arising from different

causes of action and some fact controlling, or question material to, the determination of both cases has been adjudicated against that party in the prior case." (*Buttitta,* 176 Ill. App. 3d at 882, 531 N.E.2d 957.) The relevant considerations for the application of collateral Estoppel are: (1) whether the issue decided in the prior adjudication is identical with the one presented in the case in question; (2) whether there has been a final judgment on the merits in the prior case; and (3) whether the party against whom Estoppel is asserted is a party or in privity with a party to the prior adjudication. *Ballweg v. City of Springfield* (1986), 114 Ill. 2d 107, 113, 499 N.E.2d 1373, 1375.

In the instant case, although the requirements for the third element are present, the other two elements do not appear of record sufficiently necessary to invoke the doctrine of collateral estoppel. First, the exact issue before the circuit court was not fully litigated in the prior Federal action. (*Case Presstressing Corp. v. Chicago College of Osteopathic Medicine* (1983), 118 Ill. App. 3d 782, 785, 455 N.E.2d 811, 815.) Our supreme court has determined that the party against whom Estoppel is asserted must have had a full opportunity to litigate the issue or question (*Illinois State Chamber of Commerce v. Pollution Control Board* (1979), 78 Ill. 2d 1, 7, 398 N.E.2d 9, 12), contrary to the situation here, where the first time a trier of fact ever considered evidence on the issues of proximate cause and knowledge or other factors pertaining to Touche Ross' purported negligence and breach of contract was at the trial below. Such considerations were not made in the Federal court proceeding where the court there dismissed Congregation's pendant State claims against Touche Ross. Although the findings of fact concerning the Federal securities law violations could overlap and suggest possible conclusionary determinations with respect to the State pendant claims, in the final analysis and in light of the Federal court's lack of jurisdiction, the latter claims are proper matters to be decided by the trier of fact in the State court.

Second, no determination on the merits of the pendant State claims was ever sought by Touche Ross in the Federal case, and

none was ever made by the Federal court. Moreover, dismissal of a claim for lack of subject matter jurisdiction does not constitute a final decision on the merits (*Weiland Tool & Mfg. Co. v. Whitney* (1969), 44 Ill. 2d 105, 113, 251 N.E.2d 242, 247) and thus should not serve as the basis for collateral Estoppel. See *Telegraph Savings & Loan Ass'n of Chicago v. Schilling* (1984), 105 Ill. 2d 166, 473 N.E.2d 921; *Suslick v. Rothschild Securities Corp.* (1987), 164 Ill. App. 3d 589, 517 N.E.2d 600.

Accordingly, we affirm the the circuit court's decision rejecting Touche Ross' collateral Estoppel argument with respect to findings made in the Federal proceedings brought by Congregation against securities dealers and Touche Ross.

II. Voir Dire

Touche Ross asserts that the circuit court committed reversible error when it limited the scope of *voir dire* examination regarding potential jurors' religious affiliations, contributions and attitudes. Prior to *voir dire*, Touche Ross proffered a number of questions to the circuit court to ask of potential jurors, including, in relevant part:

(1) The plaintiff in this case is an order of priests and brothers of the Roman Catholic Church, the Passionist Fathers. Is anyone here a member of the Roman Catholic Church? Is there anyone here who once was a member of the Roman Catholic Church but no longer is?

(2) Is there anyone here who has made a financial contribution to the Roman Catholic Church or to any order or institution of the Roman Catholic Church including hospitals, monasteries or schools?

(3) Have you or any member of your family ever made a financial contribution to the Passionist Fathers?

The circuit court refused to ask any of the above questions and prohibited defense council from asking them.

Touche Ross contends that because Congregation is an order of the Catholic Church and because part of the investment funds it lost came from private charitable contributions, the proffered questions were appropriate to uncover any latent bias or prejudice on the part of jurors that could affect their consideration of the evidence. Relying on decisions from other jurisdictions, Touche Ross urges that a party is entitled to discover the religious affiliations of potential jurors in cases where a religious organization is involved. *Hornsby v. Corporation of the Presiding Bishop of the Church of Jesus Christ of Latter-Day Saints* (Utah App. 1988), 758 P.2d 929, 931-33; *Casey v. Roman Catholic Archbishop* (1958), 217 Md. 595, 604-07, 143 A.2d 627, 630-32.

Congregation counters that none of the decisions relied upon by Touche Ross arose in Illinois. They urge that the circuit court properly followed the law of Illinois as applied to *voir dire* questioning.

The responsibility for *voir dire* examination lies with the trial judge and the scope and extent of this examination rests within his or her discretion. (Ill. Rev. Stat. 1987, ch. 110A, par. 234; *Kingston v. Turner* (1987), 115 Ill. 2d 445, 465, 505 N.E.2d 320, 329.) The exercise of the trial judge's discretion will not be disturbed on appeal unless the record as a whole illustrates that the judge's conduct impaired the selection of a fair and impartial jury. (*People v. Teague* (1983), 108 Ill. App. 3d 891, 894, 439 N.E.2d 1066, 1069.) The standard of review for abuse of discretion is whether the inquiry permitted created a reasonable assurance that prejudice would be discovered if present. *Friedman v. Park Dist. of Highland Park* (1986), 151 Ill. App. 3d 374, 382, 502 N.E.2d 826, 832.

In the case at bar, the transcript of the *voir dire* shows that the circuit court gave counsel permission to ask prospective jurors, *inter alia* (1) whether anyone was a member of a religious order; (2) whether a juror or any member of his family had ever been employed by any church, church related association, including hospitals and schools; (3) whether a juror or any member of his family had ever been a member of a religious organization;

(4) whether there was anyone present who would give greater weight to the sworn testimony of a member of a religious order than he would a layperson; and (5) whether it would trouble anyone if the attorney cross-examined a witness who was a member of a religious order.

Thus, in exercising its discretion, the circuit court employed means to test prospective juror impartiality, which created a reasonable assurance that prejudice would be discovered if present. (See *People v. Bunch* (1987), 159 Ill. App. 3d 494, 512 N.E.2d 748.) Unlike in *People v. Dallas* (1980), 85 Ill. App. 3d 153, 405 N.E.2d 1202, which involved nuns, the trial court below asked prospective jurors whether they would give greater credibility to the testimony of religious persons simply because of their status. (See also *U.S. v. Daily* (7th Cir. 1944), 139 F.2d 7, where the Federal court allowed inquiry as to the prejudice of prospective jurors because defendant was a Jehovah's witness, but did not allow inquiry as to the religious beliefs of the venire.) Here, the circuit court did not preclude either side from asking questions about membership in any religious organization, membership in a religious order, or employment by any religiously affiliated institution and also gave counsel an opportunity to ask about the weight a juror would give to the testimony of priests, brothers or nuns and whether cross-examination of such religious persons would be troubling. Even in a criminal case, all that is required of the trial judge is a standard inquiry into whether sympathy, bias, or prejudice would affect a potential juror's judgment or prevent him or her from being impartial. (*People v. Bunch*, 159 Ill. App. 3d at 510, 512 N.E.2d 748.) Here, Touche Ross does not point out or claim any specific prejudice on the part of the jury. Additionally, Congregation contends that Touche Ross had three unexercised peremptory challenges at the close of the *voir dire*.

Accordingly, we conclude that the circuit court did not abuse its discretion in denying Touche Ross' specific supplemental questions submitted for *voir dire* where the court-conducted and counsel-conducted examination of the venire afforded ample opportunity to discover any concealed bias or prejudice. In fact,

when it was disclosed that one of the veniremen was employed by the Archdiocese of Chicago as a school teacher and another was a minister of the United Church of Christ, the trial court permitted counsel latitude to discover any partiality on their part, listened to counsel's respective arguments and finally excused the first venireman for cause while counsel excused the second venireman by exercising a preemptory challenge. We affirm on this issue.

III. Motions In Limine

Prior to trial, Congregation made a motion in *limine* to exclude any reference to "the nature of or any problem relating to" its investments other than the accounts managed by Newell and over the objections of Touche Ross, the circuit court granted this motion. Touche Ross argues that this ruling hampered its efforts: to establish the speculative nature of Congregation's overall investment philosophy, to rebut Congregation's damage theory, and to establish an affirmative defense of contributory negligence. Touche Ross states that Congregation's theory professed if Touche Ross had reported the market value of the Newell open arbitrage positions, the unrealized losses would have been discovered as early as 1976 and Congregation would have terminated its relationship with Newell. Thus, Touche Ross urges that Congregation's investment strategy and its conduct in response to losses incurred in other investment accounts were relevant and central to the defense of this action.

Touche Ross postulates that evidence regarding Congregation's other investments would have shown that Congregation's financial officers, particularly the treasurer and investment officer, were habitual risk takers uninterested in conservative investments. They also maintain that the nature of Congregation's other investments was directly relevant to show how those investments and the Newell investments were reflected in the financial statements and that some of Congregation's other investments were not carried at market. Additionally, the circuit court's redaction of documents resulted in the presentation of documents to the jury in a grossly distorted form.

Alternatively, Touche Ross contends that the circuit court's order regarding redaction of Congregation's investments violated a well settled evidentiary principle which requires the complete presentation of evidence. (See Fed. R. Evid. 106.) Relying upon *Pridmore v. Whiting Corp.* (1932), 268 Ill. App. 592, 605, wherein the appellate court determined the circuit court committed reversible error in allowing plaintiff to offer only portions of an audit report and omit explanatory comments and certain other exhibits, (see also *Yassin v. Certified Grocers of Illinois, Inc.* (1986), 150 Ill. App. 3d 1052, 1072, 502 N.E.2d 315, 330-31), Touche Ross argues that the year end financial statements, schedules and work papers should have been admitted in their entirety.

Touche Ross also contends that the circuit court compounded the error by inconsistently applying the in *limine* order throughout the trial. For instance, although Congregation's witnesses were allowed to discuss other investments and thus opened the door on cross-examination to this line of questioning, the circuit court refused to permit Touche Ross to entertain such an inquiry relying upon the in *limine* ruling as the basis for the refusal.

Congregation asserts that the circuit court properly excluded references to other investments, which are not relevant here to contributory negligence or any other issue. Moreover, they argue that the circuit court's ruling did not materially preclude reference to other investments or prevent Touche Ross from showing the jury, if it could, that other investment securities, which had market value, were reported at cost or at something other than market value. Congregation maintains that the order merely prevented the introduction of irrelevant and confusing evidence about the nature of securities managed by other investment advisors, none of which were the subject of any claims made by Congregation against Touche Ross.

The test of an in *limine* ruling on appeal is whether the circuit court abused its discretion by excluding or allowing the evidence, and if so, whether the party suffers unfair prejudice or

the exclusion or admission of the evidence materially affected the outcome of the case. (*Ford v. City of Chicago* (1985), 132 Ill. App. 3d 408, 474, 476 N.E.2d 1232, 1237.) The decision whether or not to grant a motion in *limine* is squarely within the discretion of the circuit court (*Terracina v. Castelli* (1979), 80 Ill. App. 3d 475, 400 N.E.2d 27) and in exercising this discretion, the circuit court should balance the prejudice that might be avoided if it grants the motion against the complication or inconvenience that would result if the motion is denied. *Kerns v. Lenox Machine Co., Inc.* (1979), 74 Ill. App. 3d 194, 392 N.E.2d 688.

Because there is no error in excluding testimony which does not bear on the specific issues under consideration (*Eleopoulos v. Dzakovich* (1981), 94 Ill. App. 3d 595, 418 N.E.2d 980) and the circuit court's decision will not be reversed absent an abuse of discretion (*Behrstock v. Ace Hose and Rubber Co.* (1986), 147 Ill. App. 3d 76, 496 N.E.2d 1024), we affirm the circuit court's decision allowing Congregation's motion to exclude references "relating to investments which were not the subject of this lawsuit." First, the prevention of jury confusion, as pointed out in Congregation's brief, is recognized as a proper basis for excluding evidence which is arguably relevant. (*Fullerton v. Robson* (1978), 61 Ill. App. 3d 93, 96, 377 N.E.2d 1044, 1048.) Second, there appears to be no violation of the rule of "completeness" here. Although a party is entitled to present evidence that is relevant to its theory of the case and also to introduce evidence "which tends to show conduct inconsistent with an opponent's theory" (*Vendo Co. v. Stoner* (1982), 108 Ill. App. 3d 51, 55, 438 N.E.2d 933, 936), it does not appear that Touche Ross has met the relevancy test here. The fact that Congregation may have had problems with other investment advisors has no relevance and is not material to their claims that Touche Ross negligently failed to properly value the Newell investments.

With respect to other motions in *limine*, Touche Ross asserts that the circuit court erroneously permitted Congregation to refer to Touche Ross as a large international accounting firm and precluded Touche Ross from introducing the Federal court complaint

into the proceedings. As we have already addressed the issue with respect to the findings of fact in the Federal court proceedings, we will only address the remaining in *limine* ruling with respect to the circuit court's order allowing Congregation to refer to Touche Ross as a large firm.

Touche Ross asserts that such evidence was irrelevant to any issue in this litigation. In addition, it was highly prejudicial where Congregation repeatedly emphasized to the jury that "Touche Ross had financial specialists and consultants in every major capital in the western world." *People v. Groleau* (1987), 156 Ill. App. 3d 742, 748, 509 N.E.2d 1337, 1341.

Congregation responds that the ruling was proper in that information respecting the size and reputation of the firm is relevant to this case as Congregation hired and relied in part upon Touche Ross because of its size and sophistication. Also, mere emphasis on a party's corporate nature has been found not to constitute reversible error if it appears that no actual prejudice resulted. *Ruffiner v. Material Service Corp.* (1985), 134 Ill. App. 3d 747, 759, 480 N.E.2d 1157, 1165.

With regard to the motion "to exclude evidence of Touche Ross as a 'Big 8' accounting firm," Touche Ross has not shown that it was unfairly prejudiced by the testimony with regard to the size of the firm or the location of its offices or that the evidence materially affected the outcome of the case. The issue is whether error occurred which prejudiced the appellant or unduly affected the outcome of the proceedings. (*Bruske v. Arnold* (1969), 44 Ill. 2d 132, 139, 254 N.E.2d 453.) We do not believe that the references at issue here rose to the level of reversible error. Such evidence did not tend to evoke any bias a jury might be inclined to show against corporations generally because both parties involved were large, well-off corporate entities. The evidence does not concern the wealth of a party; nor is this a situation where a little person or victim is alleging harm on the part of a multi-mega corporation. Additionally, the jury was made well-aware of the identities of the parties. Accordingly, we affirm the circuit court's ruling.

IV. Application of Moorman

Touche Ross asserts that as there were written contracts governing the obligations of the parties for each fiscal year, it was entitled to a directed verdict on Congregation's negligence claim because it is well established that a plaintiff can not recover in tort for purely economic losses when a written contract establishes the rights and duties of the parties. (*Album Graphics, Inc. v. Beatrice Foods Co.* (1980), 87 Ill. App. 3d 338, 408 N.E.2d 1041.) Touche Ross argues that when the parties are in privity of contract, as here, the law of contract, and not tort theory, governs actions for purely economic losses and since Congregation's negligence count was simply an assertion that Touche Ross negligently breached its' contracts, such claim is barred by *Album Graphics*.

Moreover, Touche Ross continues that the Illinois Supreme Court also has recognized the fundamental difference between rules relating to recovery of economic losses in contract and tort in *Moorman Manufacturing Co. v. National Tank Co.* (1982), 91 Ill. 2d 69, 435 N.E.2d 443. Touche Ross contends that the *Moorman* holding stands for the proposition that economic losses are not recoverable in tort. Moreover, the *Moorman* holding was expanded to include professional services in *Anderson Electric, Inc. v. Ledbetter Erection Corp.* (1986), 115 Ill. 2d 146, 503 N.E.2d 246, wherein Justice Simon, in a concurring opinion, stated that to permit a party to a service contract to proceed in tort could impose obligations on a defendant going far beyond those bargained for in the contract and could subject the defendant "to a higher standard of care" and perhaps to "greater potential liability" than it intended to undertake when entering the contract. (115 Ill. 2d at 156, 503 N.E.2d 246.) Touche Ross maintains that Justice Simon's concerns were borne out here, where the jury returned two inconsistent verdicts. Because the decisional law in Illinois prevents Congregation from proceeding in tort, Touche Ross urges that it was entitled to summary judgment, directed verdict, or judgment notwithstanding the verdict on the negligence claim.

Congregation asserts that the "economic loss" doctrine has never applied to prevent tort recovery from one who is in the business of supplying information for the guidance of others in their business transactions. Congregation maintains Touche Ross fails to mention the *Moorman* exception which provides that economic loss is recoverable when one who is in the business of supplying information for the guidance of others in their business transactions makes negligent misrepresentations. (91 Ill. 2d at 88-89, 435 N.E.2d 443.) Congregation contends that the exception applies squarely to accountants with respect to negligent misrepresentations comprising the information they furnish a client to be used in the client's business transactions. For example, the *Rozny* rule (*Rozny v. Marnul* (1969), 43 Ill 2d 54, 250 N.E.2d 656), states that purchasers of residential housing can recover against a surveyor for negligently inaccurate representations of the survey. Like *Rozny*, where the only use of the survey information was to furnish guidance to persons related to their business decisions, here public accountants supply nothing but information to their clients.

With respect to the *Moorman* argument, to date, our supreme court has not squarely decided the issue before this court. Although Touche Ross' argues *Anderson* signals that the doctrine of economic loss is applicable to professional malpractice actions, Congregation's rejoins that *Anderson* fails to discuss the professional liability exception as enunciated in *Moorman* and discussed in other cases. Additionally, *Rosos Litho Supply Corp. v. Hansen* (1984), 123 Ill. App. 3d 290, 462 N.E.2d 566, decided two years before *Anderson* and involving malpractice by an architect, is not mentioned in *Anderson*. In *Rosos*, this court refused to apply *Moorman*, stating that to do so would abolish by inference all professional malpractice actions charging economic loss, arising from service contracts, based upon negligent violation of professional standards of care and skills. However, more recently, our Illinois Supreme Court affirmed the appellate court's holding that Illinois law precludes the recovery of economic losses in tort cases, including legal malpractice, which are based on claims of negligence. (*Collins v. Reynard*, Ill. Sup. Ct. Docket No. 70325

(Slip Op. October 31, 1991.) Although the court there refused to carve out an exception to *Moorman* and its progeny for attorney malpractice for recovery of purely economic losses under a tort theory of negligence unless the attorney malpractice action fit into one of the enunciated narrow exceptions; *i.e.*, where the attorney-defendant owed some extracontractual duty to the injured party or where the role of the defendant was that of a guarantor to the plaintiff; the court did reaffirm that "economic losses were to be recoverable (1) when one *intentionally* makes *false representations*, or (2) when one who is in the business of supplying information for the guidance of others in their business transactions makes *negligent misrepresentations*." (*Collins*, Slip Op. at 3 *quoting Moorman*, 91 Ill. 2d at 88-89, 435 N.E.2d 433.) (Emphasis added.) Because Congregation alleged that Touche Ross made negligent misrepresentations, the second exception to *Moorman* would apply if the other elements were found to be present. Congregation exercised its right to pursue all possible theories of recovery based on a single core of operative facts in a single proceeding (*Stolzenbach v. Pagoria* (1979), 71 Ill. App. 3d 863, 866, 390 N.E.2d 376, 378) and thus the trial court properly found it had a right of action for negligent misrepresentation in negligence or on the contract under which the information was supplied. (Restatement (Second) of Torts, Section 552, Note (g).) We believe that the trial court properly instructed the jury under each theory, contract and tort, since both theories were pleaded by Congregation and there was evidence in the record supporting each theory. Furthermore, although all malpractice by an accountant rests in some degree on a violation of the parties' contract, the courts most frequently hold accountants liable to their clients in tort (Annotation, *Accountants' Malpractice Liability to Clients*, 92 A.L.R. at 396 (1979)), and as previously stated, case law firmly establishes that the *Moorman* doctrine does extend to professionals and to professional malpractice/negligence actions under the proper factual circumstances.

Touche Ross also argues that it can not be found negligent since it followed the rules of the accounting profession and violated no binding standards. Congregation's own experts agreed

with Touche Ross' accounting expert that no authoritative opinion or statement requires debt securities to be recorded at market value on the financial statements. Touche Ross contends, then, that the mutual decision by the parties to report the Newell open arbitrage positions at net cash was appropriate; thus, Touche Ross was entitled to a directed verdict on the negligence count because the jury verdict rendered holds them to a higher standard than that recognized in the profession as a whole.

Congregation rejoins that it proved the standard of care required of professional accountants through expert testimony, and such standard is recognized as a very high level of professional responsibility. (*Margolies v. Landy & Rothbaum* (1985), 136 Ill. App. 3d 635, 638, 483 N.E.2d 626, 629.) Here, they argue, the evidence shows that Touche Ross negligently misrepresented that it was reporting the Governments at market and presented inaccurate financial statements although the basic objectives of financial statements is to provide information to the clients useful for making economic decisions. Further, there was ample testimony that Touche Ross had violated generally accepted accounting principles. The law of negligent misrepresentation involves a breach of the duty to use due care in obtaining and communicating information upon which others may reasonably be expected to rely in the conduct of their economic affairs. (*United States v. Neustadt* (1961), 366 U.S. 696, 6 L. Ed. 2d 614, 81 S.Ct. 1294.) A misrepresentation can result from the failure to provide adequate information when there is a duty to provide such information as well as providing information which is false. (*Leaf v. United States* (9th Cir. 1981), 661 F.2d 740, 742.) A negligent misrepresentation is a representation that the maker believes to be true, but because of negligent expression, is in fact false. *Luciania v. Bestor* (1982), 106 Ill. App. 3d 878, 888, 436 N.E.2d 251.

With respect to the parties' arguments about the several issues applicable to a negligence action against an accountant and the sufficiency of the evidence in the present case, our courts have found that the question of proximate causation in accounting

malpractice actions, as in all negligence actions, is a question for the jury to be determined from all the attendant circumstances. (*First National Bank v. Brumleve & Dabbs* (1981), 183 Ill. App. 3d 987, 992, 539 N.E.2d 877, 880.) Here, a review of the record shows that the evidence heard by the jury supported its verdict against Touche Ross. The language in the "investments" paragraph which required Touche Ross to inspect and confirm securities, was presented to the jury in addition to the disclaimers found in the footnotes to the Financial Statement. Further, the record shows that Melchert admitted "major errors" in the reports. Accordingly, upon reconciliation of the *Moorman* issue, we find that the record supports the jury's verdict on the negligence count.

V. Jury Instruction on Negligent Misrepresentation

In the alternative, Touche Ross urges that the circuit court committed reversible error by denying motions for a directed verdict and judgment N.O.V. on the negligence count when Congregation, after the close of all the evidence, abandoned the claim that Touche Ross had made "negligent misrepresentations and omissions in its Reports on Review of the Financial Statements." They assert that Congregation amended the complaint to delete any reference to negligent misrepresentation because it had failed to prove at trial that Congregation relied upon alleged misstatements of the market value of the arbitrage positions in the reported and financial statements.

Congregation counters that it did not abandon the negligence claim, but merely amended the complaint to conform the allegations to the evidence. (*Gordon v. Bauer* (1988), 177 Ill. App. 3d 1073, 532 N.E.2d 855.) They assert that counsel merely responded to the nature of the negligence claim when Touche Ross asked the court for jury instructions that in order to prevail, Con gregation had to prove Touche Ross *intended* that its misstatements would be relied upon by the Congregation.

We have reviewed the record and found that the original negligence count against Touche Ross contained allegations for

negligent misrepresentation and these allegations were realleged in all material aspects in the amended complaint. Congregation contended and the court accepted the proposition that additional allegations of negligent misrepresentations should be added and certain repetitive allegations deleted to avoid confusion when read to the jury in the issue instruction. Because the circuit court required the issue instruction to contain verbatim, the claims and affirmative defenses as pled by each party, both parties filed amended pleadings during the issues conference. Accordingly, as we believe that the amended complaint properly contained all material allegations of negligent misrepresentation and in any event, vague, unintentional, oral statements of counsel will not operate as a waiver of the allegations contained in the pleadings (see *Melrose Park National Bank v. Melrose Park National Bank* (1984), 123 Ill. App. 3d 282, 462 N.E.2d 741), we affirm the circuit court's denial of Touche Ross' motions for directed verdict and judgment notwithstanding the verdict on this question. Moreover, "[a] pleading may be amended at any time, before or after judgment, to conform the pleadings to the proofs." Ill. Rev. Stat. 1989, ch. 110, par. 2-616(c).

VI. Congregation's Knowledge and Consent

Touche Ross argues that the manifest weight of the evidence establishes that Congregation consented to the accounting method used to report the Newell open arbitrage positions because both Father Parsons and Bro. Kent testified to a meeting with two accountants from Touche Ross in which the parties agreed that the Newell investments would be reported at margin or net cash and the financial statements are entirely consistent with this agreement. Further, Touche Ross only agreed to prepare unaudited financial statements, of which the summary of investment activity schedule was not a part and Sr. Flaherty knew the schedules did not contain market value figures because she herself gave them to Touche Ross each year to be included in the annual report as additional information with the instruction not to report the open positions at market value.

Touche Ross next asserts that even if the investment paragraph of the engagement letter had been applicable here, Congregation waived application of that provision by agreeing with them that the open arbitrage positions would not be reported at market value and when it did not question the manner in which the investments were reflected in the financial statements although that reporting method was clearly disclosed in a footnote to the financial statements. Touche Ross also raises the argument that Congregation was estopped from alleging that the open arbitrage positions should have been reported at market.

Congregation contends that the jury properly rejected the defenses of consent and waiver and that there was no basis for estoppel here. They argue that to prevail on any of these theories, Touche Ross must have established that Congregation intentionally and knowingly agreed that the value of the Newell investments would be reported at meaningless values, rather than at their actual or market value, despite the annual promises in the engagement letters to do the opposite. Contrary to Touche Ross' assertions, neither Bros. Parson nor Kent ever agreed that the value of the investments would be reported at anything other than their real (or market) value. They claim that both men testified that Touche Ross recommended a method of accounting and that Melchert always believed that cost was substantially equal to market and repeatedly advised the Provincial Council members of this belief.

In *Sexton v. Smith* (1986), 112 Ill. 2d 187, 193, 492 N.E.2d 1284, the Illinois Supreme Court defined the doctrine of waiver as the "intentional relinquishment of a known right." In the present case, Touche Ross was allowed to fully present evidence on its defenses and the circuit court properly instructed the jury that if it believed that Touche Ross had proved the defenses, its verdict should be for Touche Ross. Further, there was conflicting evidence whether the contract had been performed according to its terms and whether the conduct of Congregation constituted a waiver of a known right delineated in the contract.

Accordingly, we find that evidence of the applicability of the investment paragraph contained in the engagement letter contract and discussions between Congregation officers and Touche Ross employees and its managing partner concerning the Newell arbitrage investments presented a jury issue as to whether Touche Ross was at fault when it not only failed to report the investments at margin or net cash, but also when it failed to physically inspect, confirm or test the market value of the investments by reference to published market quotes as required by the engagement letter contract prior to each year-end report. Moreover, conflicting evidence as to whether Congregation accepted the information contained in the reports by agreeing to report the Newell arbitrage investments in a particular manner was a jury question. Additionally, conflicting evidence as to whether Congregation had knowledge that such information and reporting reflected a value of the investments less than their real or market value, coupled with knowledge that such conduct by Touche Ross constituted a breach of the engagement letter contract so as to waive such breach was also a question for the jury. The resolution of those issues rests on the credibility of the witnesses and the jury, as the trier of fact, was in the best position to weigh the evidence and observe and assess the credibility of the witnesses. As findings of fact by the jury will not be disturbed unless contrary to the manifest weight of the evidence (see *Hartwig Transit, Inc. v. Menolascino* (1983), 113 Ill. App. 3d 165, 446 N.E.2d 1193), we decline to reverse the trial court's denial of Touche Ross' motions for directed verdict and judgment notwithstanding the verdict.

VII. Other Jury Instructions

Touche Ross also contends that the circuit court committed prejudicial error by refusing jury instructions tendered by it, including, but not limited to instructions: concerning the scope of an agent's authority; explaining that an agent's knowledge is imputed to his principal; setting forth the elements of a cause of action based upon negligent misrepresentation; relating to the elements necessary to establish a breach of contract claim; explaining that a written agreement may be modified by a

subsequent oral agreement; concerning the doctrine of waiver; explaining the doctrine of equitable Estoppel; and relating to the findings of fact made by the Federal courts.

We have reviewed the relevant portions of the record and the parties' arguments made at the issues and instructions conference and conclude that the jury was correctly instructed for purposes of this trial and further any error that may have occurred in disallowing Touche Ross' proffered instructions did not constitute reversible error. Where no prejudice is shown, our courts have held that refusal to give an instruction is not reversible error. (*Goodrick v. Bassick Co.* (1978), 58 Ill. App. 3d 447, 453-54, 374 N.E.2d 1262.) A review of the court's decision to disallow certain instructions shows that the instruction was rejected either because no proof had been offered at trial with respect to the giving of such instruction; because it would have been misleading to the jury; because it was an inaccurate statement of the law; because it was argumentative; because it did not follow the applicable IPI rules; or because other instructions adequately covered a given subject.

VIII. Contributory Negligence

With respect to alleged erroneous post-trial rulings made by the circuit court, Touche Ross first asserts that the circuit court should have granted a new trial on Congregation's negligence count because the manifest weight of the evidence establishes that Congregation was contributorily negligent by making improvident investment decisions. They assert that Congregation failed to properly monitor Newell's activities, gave him unbridled discretion, and allowed him to continue to engage in arbitrage trading even after learning that the market value of his account was substantially less than he had represented. They contend that minimally, the jury should not have found Touche Ross liable for the additional $500,000 Congregation invested with Newell on April 14, 1981, after learning of the losses already incurred and further that the amount of damages incurred by Congregation at that time was under $1 million.

The question of contributory negligence is a question of fact for the jury and its determination here must stand unless all of the evidence, when viewed in a light most favorable to Congregation, overwhelmingly favors this defendant so that no contrary verdict based on this evidence could ever stand. *Gruidl v. Schell* (1988), 166 Ill. App. 3d 276, 281, 519 N.E.2d 963.

IX. Refusal to Consent to Remittitur of Damages

Touche Ross contends that a remittitur reducing a jury verdict is appropriate when the circuit court concludes, as it did here, that the damages awarded by the jury are excessive and that they do not conform to the evidence adduced at trial. (*Wall v. Amoco Oil Co.* (1981), 92 Ill. App. 3d 921, 925, 416 N.E.2d 705, 708-09.) They assert however, as here, after the circuit court orders a remittitur and the plaintiff fails to consent to such order, defendant is entitled to a new trial. (*Prochot v. Drew* (7th Cir. 1960), 283 F.2d 904, 905.) However, Touche Ross says that the intent of the jury can not be ascertained here as shown by the inconsistent verdicts and award of damages. Moreover, the judgment of the circuit court is also inconsistent where the order entered a liability, but no money judgment on the contract verdict.

Congregation distinguishes the cases cited by Touche Ross and contends that none of them support a request for a new trial. They assert that the judgment here, as remitted by the circuit court, is supported by the evidence and any inconsistency between the jury's awards on the counts involves the amounts only. Congregation contends that the judgment order entered below correctly reflects the jury's award of the full measure of damages to it. The Judgment provides:

> "ORDERED that judgment is entered on the verdict of the jury on Counts I and III finding the defendant *** liable to plaintiff for accounting malpractice-negligence (Count I) and breach of contract (Count III).
>
> * * *

> JUDGMENT
> IT IS ORDERED that plaintiff *** have final judgment against and recovery against defendant *** in the principal amount of $3,819,352.00, plus interest *** and taxable costs of $3,858.67."

If after considering all the evidence, the trial judge concludes that the jury verdict is excessive, the judge may allow the verdict to stand but must act to correct the injustice; and the failure to do so is, itself error. (*Hedrich v. Borden Co.* (1968), 100 Ill. App. 2d 237, 241 N.E.2d 546.) The trial court can rectify an excessive award by ordering a remittitur, which is an agreement by the plaintiff to relinquish, or remit to the defendant, that portion of the jury's verdict which constitutes excessive damages (*Anderson v. Greyhound Lines, Inc.* (1975), 34 Ill. App. 3d 643, 339 N.E.2d 465), and to accept the sum which has been judicially determined to be properly recoverable damages. *Bart v. Union Oil Co.* (1989), 185 Ill. App. 3d 64, 540 N.E.2d 770.

It is established in Illinois, however, that the trial court does not have the authority to reduce the damages by entry of a remittitur if the plaintiff objects or does not consent. (See *Foster v. Springfiled Clinic* (1980), 88 Ill. App. 3d 459, 410 N.E.2d 604.) Additionally, it is well settled that a plaintiff's refusal to consent to remittitur will result in the trial court ordering a new trial. (See *McCausland v. Wonderly* (1870), 56 Ill. 411; *National Malleable Castings Co. v. Iroquois Steel & Iron Co.* (1929), 333 Ill. 588, 165 N.E.199.) In the present case, Congregation filed a "Statement of Non-Consent to Remittitur" professing its outright refusal to accept the trial court's remittitur of the jury's verdict in the amount of $1,500,000 on the breach of contract count to $0. Congregation contends that although it can not recover twice for the same injury, the verdict on the contract count can be raised to the same amount as the award on the negligence count. Touche Ross, however, maintains that the obvious inconsistency between the measure of damages awarded under two separate claims for relief mandates a new trial.

As previously discussed, the law on the issue is well settled. Congregation's own expert, Mr. Vincent Sparrow, calculated their damages. Although the jury's verdict on the negligence count was $3,900,000, the trial court properly reduced that verdict to $3,819,352 to conform to the evidence presented at trial and primarily based upon Mr. Sparrow's testimony. The problem, however, arises with respect to the verdict of $1,500,000 on the breach of contract count. While the jury may have intended liability against Touche Ross on both counts, Congregation obviously can not recover twice for the same injury. Accordingly, we will affirm the judgment of the trial court with regard to the remittitur of the negligence count from $3,900,000 to $3,819,352 and with regard to the reduction of the breach of contract verdict from $1,500,000 to $0 on the condition that plaintiff files a consent to the remittitur with the clerk of this court pursuant to Supreme Court Rule 366(a)(5). (107 Ill. 2d R. 366(a)(5).) In the event such consent is not filed within the 30 day period, the judgment is reversed, and the case is remanded to the trial court on the issue of damages.

We have reviewed each of the other purported trial errors presented by Touche Ross and find them to be meritless as to warrant further discussion or consideration by the court.

CONGREGATION'S CROSS-APPEAL

Prejudgment Interest

On its cross-appeal, Congregation raised three issues. First, it contends that it is entitled to prejudgment interest as a matter of law. (Ill. Rev. Stat. (1989), ch. 17, par. 6702.) Additionally, courts allow awards of prejudgment interest to fully compensate an injured party for all damages incurred from the time the injury is sustained to the date upon which judgment is entered. *West Virginia v. United States* (1987), 479 U.S. 305, 309, f.n. no. 2, 107 S. Ct. 702, 706; *In re Estate of Wernick* (1989), 127 Ill. 2d 61, 75, 535 N.E.2d 876, 888.

Touche Ross responds that the circuit court correctly concluded that Congregation was not entitled to prejudgment interest

on the amounts awarded by the jury. This court has recently reaffirmed that "there is no right to recover prejudgment interest unless it is permitted by statute or there is an agreement between the parties." (*Alguire v. Walker* (1987), 154 Ill. App. 3d 438, 447, 506 N.E.2d 1334, 1341.) The record does not reflect the existence of an agreement between the parties governing prejudgment interest and it is well settled that under Illinois statutes, there is no authorization for prejudgment interest in tort cases. (*Northern Trust Co. v. County of Cook* (1985), 135 Ill. App. 3d 329, 336, 481 N.E.2d 957, 962.) Moreover, even if the statute did apply here to the breach of contract claim, the judgment appealed from reflects no monetary award to which interest may be attached. Accordingly, we affirm the trial court on this issue.

Breach of Fiduciary Claim

Congregation next asserts that the circuit court erred because abundant evidence exists in the record to support the breach of fiduciary claim. Touche Ross asserts that no Illinois court has held that a fiduciary relationship exists between an accountant and his client as a matter of law and here Congregation failed to present any evidence that Touche Ross ever exercised any influence, or domination and control over their investment decisions. (*In re Estate of Shedrick* (1984), 122 Ill. App. 3d 861, 866, 462 N.E.2d 581, 585.) They contend that the evidence shows Congregation monitored Newell and looked to its own financial advisors, not Touche Ross for investment advice.

The standard of review when considering the propriety of a circuit court's decision to direct a verdict, is whether the evidence, when viewed in its aspect most favorable to plaintiff, so overwhelmingly favors defendant, that no contrary verdict based on the evidence could ever stand. (*Rockett v. Chevrolet Motor Div. General Motors Corp.* (1975), 31 Ill. App. 3d 217, 220, 334 N.E.2d 764, 768.) Here, although the parties agreed to specific conditions involving review of the Newell securities and investments, the overall accounting and review process relationship between the parties did not involve an auditing arrangement whereas those cases that found a fiduciary relationship between

an accountant and client involved strictly auditing situations. Thus, we affirm.

Increase of Monetary Judgment on Breach of Contract Verdict

Congregation argues that the circuit court was implored to increase the breach of contract damages by entry of judgment notwithstanding the verdict or, in the alternative, by modifying it to conform to the intent of the jury and comport with the evidence. They urge that no jury intent can be found in the present record to in any way limit the damages awarded for breach of contract to a sum below the amount of the malpractice award. Congregation, thus asks this court to modify the verdict on the breach of contract count to provide damages of $3,819,352 in accordance with its authority to so amend pursuant to Supreme Court Rule 366(a)(1).

Touche Ross counters that judgment notwithstanding the verdict to increase the damages awarded on Congregation's breach of contract count would be inappropriate. Essentially, Congregation is requesting an order of additur, which, Touche Ross must consent to in lieu of receiving a new trial. (*J.I. Case Co. v. McCartin-McAuliff Plumbing & Heating, Inc.* (1987), 118 Ill. 2d 447, 456, 516 N.E.2d 260, 265.) Touche Ross concludes that as it represented to the circuit court that it would not provide such consent, absent affirmance of the circuit court's order of remittitur on the breach of contract claim to $0, this court should order a new trial.

As discussed above, we are not satisfied with the trial court's decision with respect to the remittitur issue. Furthermore, we are less satisfied with Congregation's contention that additur is an appropriate solution to this problem. Accordingly, as above stated, we will follow the mandate of Supreme Court Rule 366(a)(5), and absent the consent of entry of remittitur by Congregation, this cause is then remanded to the trial court on the issue of damages.

AFFIRMED IN PART, AND REMANDED WITH INSTRUCTIONS.

CAMPBELL and BUCKLEY, J.J., concur.

APPENDIX C

IN THE UNITED STATES DISTRICT COURT

Northern District of Illinois
Eastern Division

Congregation of the Passion, Holy Cross Province, a not-for-profit corporation, *Plaintiff.* *vs.* Kidder Peabody & Co., Inc., a foreign corporation, et al., *Defendants.*	Docket No. 81 C 3159 Chicago, Illinois September 21, 1984 10:00 o'clock a.m.

TRANSCRIPT OF PROCEEDINGS
BEFORE THE HONORABLE CHARLES P. KOCORAS

APPEARANCES:

For the Plaintiff:	MR. THOMAS WARD MR. DAVID GUSTMAN
For the Defendants:	MR. JOE A. SUTHERLAND MR. DANIEL D. BARR MR. KURT SCHULTZ MS. MARY P. BENZ MR. FRANK HIGGINS MR. DOUGLAS SIDDOWAY
Court Reporter:	MS. JOENE HANHARDT

THE CLERK: 81 C 3959, Congregation of the Passion vs. Kidder Peabody. Ruling.

MR. WARD: Good morning, your Honor, Thomas Ward for the plaintiff.

MR. GUSTMAN: Good morning, your Honor, David Gustman for the plaintiff.

MR. SUTHERLAND: Joe Sutherland for Kidder Peabody.

MR. BARR: Dan Barr on behalf of Touche, Ross & Company.

MR. SCHULTZ: Good morning, your Honor, Kurt Schultz for First Boston Corporation.

MS. BENZ: Mary Pat Benz on behalf of Bankers Trust.

MR. HIGGINS: Frank Higgins on behalf of Touche, Ross, your Honor.

THE COURT: Good morning.

MR. SIDDOWAY: Douglas Siddoway on behalf —

THE COURT REPORTER: I am sorry, I cannot hear you.

MR. SIDDOWAY: Douglas Siddoway.

THE COURT: Do we have everybody?

(No response.)

THE COURT: Okay.

Presently before me are the motions for summary judgment of the four dealer defendants and Touche, Ross. I will first address the dealer defendants' motions.

The allegations underlying this lawsuit and the factual materials which have been disclosed during exhaustive discovery are well known to all of you, and I will not repeat them here. They have since become rather well known to me, too.

All parties involved in the present motions agree that the losses suffered by the plaintiff are regrettable, and that is my sentiment exactly, as well, the moving defendants contend, however, that others caused plaintiff's losses and that they should not be held liable. Both sides have done an excellent job of briefing the motions, and for that I do commend all of you. After

reviewing the briefs and the supporting appendices, I find that summary judgment should enter in favor of the dealer defendants. My reasons are as follows.

First, I find that the dealer defendants cannot be held directly liable under Counts 1 through 4 for fraudulent misrepresentations.

As the Supreme Court made clear in both the Affiliated Ute Citizens and Chiarella cases, liability for non-disclosure "is premised upon a duty to disclose arising from a fiduciary relationship of trust and confidence between parties to a transaction."

Thus, the defendants were under no obligation or duty to disclose material facts to plaintiff unless the facts establish that they had a fiduciary relationship.

According to the law of this Circuit expressed in the Avern case, a fiduciary relationship does not automatically arise, as a matter of law, between a broker/dealer and its customers; authority to the contrary from other jurisdictions is not persuasive. Thus, I am required to assess the particular facts of this case; if they reveal that no fiduciary relationship existed, under the authority of Shearson, that issue need not be reserved for a jury trial.

The undisputed facts of this case establish that plaintiff never sought nor received advice of any kind from the dealer defendants. Investment decisions were made by plaintiff's investment adviser Newell — in whom they had entrusted full discretion — and were tracked by plaintiff's officers and other advisers. There were no contacts or communications whatever between the dealer defendants and plaintiff, except that each dealer defendant mailed the confirmation slips — of undisputed accuracy — to plaintiff or Newell.

Unlike the Rolf case, the dealer defendants did not recommend Newell directly to plaintiff, nor did they in any way reassure plaintiff that Newell's investments were suitable. There was no lulling here. Defendants' financing of the transactions did not

"lull" plaintiff within the meaning of Rolf; their financing was simply an integral part of their execution of Newell's orders.

I also find it insufficient for plaintiff to imply that it relied on the dealer defendants and they owed plaintiff a concomitant duty to disclose simply because defendants were well-known firms, transacted substantial business with plaintiff, and earned profits from those transactions. No such rule of law exists, and none should; our financial system cannot operate if large brokerage houses cannot execute orders placed with them by independent expert advisers without first exercising a fiduciary duty to examine the suitability of the transactions.

Finally, plaintiff fails to raise any material issues of fact concerning Newell's purported "dual agency". As the Seventh Circuit recently stated in Korf vs. Ball State, a material issue of fact is one which would be outcome determinative. Plaintiff's facts do not meet this standard. Proof of friendships or mutually satisfactory business relations between an investment adviser and a broker/dealer does not establish the existence of an agency agreement. The facts show that Newell was plaintiff's agent only.

Based on the foregoing evidence in the record, I hold that the relationship which plaintiff had with the dealer defendants did not impose a fiduciary obligation on them to seek out plaintiff and disclose to it that Newell's investments were probably or perhaps unsuitable.

I likewise find that the defendants made no affirmative material misrepresentations to plaintiff. Plaintiff never asserts that any of the confirmation slips were in any way inaccurate, and defendants emphasize that plaintiff never came to defendants with any questions about the slips. Plaintiff was able to track the investments based on the slips. Moreover, the defendants knew that plaintiff had hired an investment adviser who clearly was able to understand the confirmations.

In these circumstances, as in the Fifth Circuit Warren case, plaintiff cannot prove a 10(b) misrepresentation simply by saying that it was confused. Although this Court held in Cant that

confusing slips constituted misrepresentations, the Court stressed that liability arose due to the "special circumstances" of that case; mainly, the "dependant relationship" which the small investor had on his broker. No such reliance existed here. The reliance, very frankly, was on Newell. Plaintiff had hired a knowledgeable adviser and received additional assistance from various boards of advisers who reviewed its investments. Defendants cannot be penalized because the transactions chosen by plaintiff were complex; and, therefore, although accurately reported, might have been confusing.

Finally, as Judge Aspen explained in Issen, there is no duty to describe accurate facts in a pejorative manner.

For these reasons, I find that the dealer defendants did not violate Section 10(b); they had no duty to disclose purported material information to plaintiff and they did not make any affirmative misrepresentations.

The remaining federal securities allegation against the dealer defendants states that they aided and abetted Newell in his violations of the federal securities laws.

As all parties agree, in order to prove aiding and abetting, plaintiff must first establish a primary violation by Newell. Because I agree with defendants that the Seventh Circuit's O'Brien decision precludes such a finding of primary liability, the aiding and abetting count must fail.

The record of this case shows that Newell was given—and I quote his agreement found at FBX 2—"Full discretion to develop and implement plaintiff's investment policy." Likewise, in nearly every other way the agreement with Newell parallels that which was at issue in O'Brien. The one exception was plaintiff's ability to add or withdraw funds from the account over which the adviser had full discretion. Having that authority, however, did not give plaintiff an investment decision in connection with the purchase or sale of a security.

Although the Seventh Circuit held in Goodman that the plaintiff's decision to commit additional funds to a limited partnership agreement did constitute an investment decision in connection with the purchase of a security, the Goodman court had first ruled that the partnership agreement was itself a security.

In contrast, our Circuit explicitly stated in Hirk that a discretionary investment account, such as that into which plaintiff inserted more funds, is not a security. Thus, I am taken back to the holding of O'Brien.

Finally, even if I were to find that a primary violation against Newell could be proven the teachings of Rolf as expressed in the footnote added after a rehearing en banc, would require the entry of a judgment in favor of the defendants. No liability for aiding and abetting is imposed on a broker/dealer who merely executes an unsuitable investment decision for an investment adviser with sole discretion over plaintiff's account. That is exactly what occurred here. Even if Newell's conduct was fraudulent, there is no evidence to support the notion that the moving defendants aided and abetted that fraud. Judgment must enter for the dealer defendants on the federal securities claims.

The only federal claim lodged against Touche, Ross is also premised on the aiding and abetting theory. My earlier discussion regarding O'Brien, and the lack of a primary violation, also precludes a finding of liability against Touche, Ross.

Additionally, there is no evidentiary basis to conclude that Touche, Ross aided or abetted Newell in anything he did, let alone a securities fraud scheme.

The remaining claims are all state law causes of action. Because this Court is one of limited jurisdiction, and a state court could as easily preside over the remaining issues, I will decline to exercise pendent jurisdiction over these matters and hereby dismiss them.

That, unfortunately for the plaintiff, in my view is the necessary outcome of the motions, Mr. Ward. I know a lot of

money was lost here, but the law requires first some responsibility before there can be some accounting, and I dare say in all of the papers that were submitted to me I could not find that. It is an unfortunate situation. What can I say? There was a lot of money involved and a lot of money lost—a lot of money lost for good purposes. I am not unmindful of that; but, by the same token, we cannot say to the accounting firm and the broker/dealers, "Because there was this horrible mishap we are going to look to you, either because of your size or because you were out on the other end of these transactions or executing the orders that you have an obligation to pay."

It is unfortunate, but I have looked at the papers carefully and there was not any way it could come out other than that, very frankly.

So, that is what I did.

MR. SCHULTZ: Thank you, your Honor.

MR. SUTHERLAND: Thank you, your Honor.

Your Honor, we should mention to you, I think that the dealer defendants also have counter claims still pending for the debit amounts in the account and we will be coming in in the near future.

THE COURT: I am aware of that, as well as the fact that—and I am not quite sure what happens to those, frankly. I am aware that Newell and Bianchina—or however you pronounce it—

MR. WARD: Bianchina.

THE COURT: —they are still here. So, I do not know where we go from there.

MR. SUTHERLAND: We will talk among ourselves and—

THE COURT: All right.

MR. SUTHERLAND: —I think we will be coming back in on motions for summary judgment on the deficits.

THE COURT: Well, why do you not have a discussion among yourselves—both among yourselves and with Mr. Ward; I do not know what he intends to do—by way of the future course of this case, either by way of appeal or by pursuit of the remaining defendants or whatever. So, I think you need to sort that out.

MR. SUTHERLAND: We will do that, your Honor.

THE COURT: And perhaps you can report back to me. I do not want you to loose any time. So, you tell me when you want to come in and tell me what you view the future course of this case to be.

MR. SUTHERLAND: In about a week? Two weeks?

THE COURT: This does not dispose of the whole case, so I do not think you have a clock running on any appeal—if that is—

MR. WARD: I think two weeks would then be a reasonable time.

THE COURT: All right.

Again, I am—look, as a human being, I am very sorry that all of this happened—and I do not mean to apologize for my decision, but I want you to know it is not unrecognized that there were tremendous hardships here. I feel bad about that. Look, the plaintiffs in this case are doing literally the Lord's work. Not everybody does the Lord's work. So, if there should be some victim, it should not be them. I did not put the players together or these transactions.

I guess I feel so bad, but I'm trying to tell you that.

MR. WARD: I understand.

THE COURT: It could not come out any other way.

MR. SCHULTZ: Thank you, your Honor.

MR. SUTHERLAND: Thank you, your Honor.

THE COURT: We will have you back in two weeks for some further report on the status of this case.

THE CLERK: October 5th.

MR. HIGGINS: Your Honor, can I get a copy of your opinion?

THE COURT: I will not issue a written opinion, so you will have to order it through my court reporter.

* * *

I certify that the foregoing is a correct transcript from the record of proceedings in the above-entitled matter.

Attest:

/s/ Joene Hanhardt,
Official Court Reporter

September 24, 1984

APPENDIX D

IN THE UNITED STATES DISTRICT COURT

Northern District of Illinois
Eastern Division

Congregation of the Passion, Holy Cross Province, a not-for-profit corporation, *Plaintiff.* *vs.* Kidder Peabody & Co., Inc., a foreign corporation, et al, *Defendants.*	Docket No. 81 C 3159 Chicago, Illinois April 30, 1985 10:00 o'clock a.m.

TRANSCRIPT OF PROCEEDINGS
BEFORE THE HONORABLE CHARLES P. KOCORAS

APPEARANCES:

For the Plaintiff:	MR. THOMAS WARD
For the Defendants:	MR. JOE A. SUTHERLAND MR. JEROME POPE MR. MICHAEL FORTI MR. FRANCIS EVEN MS. MARY PATRICIA BENZ
Court Reporter:	MS. JOENE HANHARDT

THE CLERK: 81 C 3159, Congregation of the Passion v. Kidder Peabody. Ruling.

MR. SUTHERLAND: Good morning, your Honor, Joe Sutherland for the defendant Kidder Peabody & Company.

MR. FORTI: Good morning, your Honor, Michael Forti representing the defendant Touche, Ross and Company.

MR. POPE: Jerry Pope for the defendant First Boston.

MS. BENZ: Mary Patricia Benz on behalf of defendant Bankers Trust.

THE COURT: Here comes Mr. Ward.

MR. WARD: Good morning, your Honor, Thomas Ward for the plaintiff.

THE COURT: You are only 10 seconds late. We just called the case.

Do we have anybody else coming?

MR. SUTHERLAND: Not that I know of, Judge.

THE COURT: All right.

This matter comes before the Court on the defendants' motion for summary judgment on their counterclaims against the plaintiff, the Congregation of the Passion. The defendants are Kidder Peabody & Company, the First Boston Corporation, Bankers Trust Company and Briggs, Schaedle and Company -- referred to collectively as the dealer-defendants. The plaintiff opposes the dealers' motion and has filed a cross-motion for summary judgment.

In its complaint against these four dealers, the plaintiff sought to recover investment funds which it had committed to its investment agent, Cranford Newell. The agreement between the plaintiff and its agent gave him full discretion to effect arbitrage transactions and letters sent to the dealers by the plaintiff requested them to accept and execute orders placed by Newell for the accounts of the plaintiff.

On September 21, 1984, this Court found that the plaintiff could not recover against the dealers for alleged violations of Section 10(b) and Rule 10b-5. Summary judgment on those claims was granted in favor or the dealers.

The counterclaims at issue today allege an action to collect sums from the plaintiff as a result of various securities transactions. The dealers state that before May, 1981, the plaintiff, through its agent, entered into arbitrage contracts with them to buy or sell government and federal agency securities.

On May 7, 1981, Kevin O'Malley, director of the Congregation of the Passion, ordered the dealers to close out all the open positions in the Congregation's accounts. All four defendants allege they have unsuccessfully demanded of the plaintiff the amounts due them as a result of the close out. The amounts are: Bankers Trust, $743,128.57 plus interest of $131,625.38; First Boston, $1,202,775.09 plus interest of $205,474.05; Briggs, $349,870.57 plus interest of $60,958.42; and Kidder, $956,531.53 plus interest of $167,393.02.

The nature of the series of complex transactions which Newell conducted from July, 1975 through May, 1981 are described in the complaint at Paragraphs 9 through 21. The plaintiff describes how Newell established accounts with the four dealers and began arbitraging United States Government bonds and other debt securities. Both parties define arbitraging as the simultaneous purchase and sale of the same or equivalent security in matched and offsetting principal amounts of the same or different markets to profit from the price discrepancies. Throughout these transactions, each one was clearly identified and known to each of the dealers as for the account of the plaintiff.

Plaintiff further alleged that through its agent's repurchase agreements and other devices, the plaintiff was placed at risk for many millions of dollars beyond its investment funds. As a result of these transactions, Kidder made a demand upon plaintiff and after investigation on May 6, 1981, plaintiff ordered each defendant to cover all open positions and sustained losses as a result.

Accepting all of these facts as true and viewing them in the light most favorable to the plaintiff, the Court turns to the plaintiff's argument in opposition to summary judgment for the amounts allegedly due and owing. Plaintiff seeks to make a distinction between its agent's loss of its retirement funds through arbitrage transactions and loss of funds which plaintiff describes as lost, not through arbitrage, but other highly leveraged transactions entered into by Newell and the dealers alone using funds loaned by the dealers to Newell.

This is an argument of several related steps: Plaintiff must show that all of the latter transactions were without its knowledge or consent, that the cash transactions flowing into and out of their accounts were loans to their agent and that the agent began in arbitrage transactions, but abruptly stopped after the investment funds were lost.

The plaintiff argues that Newell is an agent without authority for the latter transactions and that the dealers must look exclusively to him to recover the losses sustained at the close out. Finally, whatever the outcome of the legal question, the plaintiff argues that the exact amount of the losses is disputed and that this created a disputed fact which precludes summary judgment for the dealers.

The plaintiff's position, however, contradicts the facts set forth in its complaint and the documentation and nature of the series of transactions at issue. First, the plaintiff gave Newell, as its agent, full discretion to effect arbitrage transactions for its account and directed the dealers to accept his orders on their behalf.

As this Court held earlier, the dealers were under no obligations to plaintiff to determine if Newell's transactions were appropriate for a religious order or were wise decisions or were decisions that placed the plaintiff at terrible risk.

Simply put, Newell had broad discretion and the plaintiff had knowledge of his activities which it cannot deny. During the

years 1975 through 1981, plaintiff was able to track the investments through confirmation slips and accurate reports of the transactions which the dealers supplied. Plaintiff received the statements of its United California Bank account and also had before it those statements, the cash sheets and the ticket numbers assigned by Newell for each transaction. The cash transfers were not going into the agent's hands while the principal remained unaware.

In this case, the funds in question were flowing in and out of the plaintiff's own bank account. Therefore, plaintiff was not without knowledge of Newell's transactions during this period of further losses. The documents and the transactions were complex, confusing and ultimately unwise, but the plaintiff had the ability to follow them and to have review of them for themselves or by another specialist other than Newell.

Second, the transfers involved were not loans made by the dealers to the agent Newell. As plaintiff described the transactions, the dealers would settle in cash for the difference between the long debit and the short credit on the arbitrage and the amount would be wired to its account. Plaintiff's receipt of cash on opening an arbitrage was the result of that transaction and not a loan made through their agent which they kept, but which he was responsible for repaying.

Moreover, the funds were in the plaintiff's account, not the agent's. The fact the dealers viewed Newell as their client does not change the nature of the transaction. Newell had been the agent for plaintiff and the client to the dealers from the start of the transactions. However, as plaintiff admits, it had never been more than a name on the slip to the dealers all along and the dealers were never required to inquire into plaintiff's particular situation.

Third, Newell was not an agent acting without authority or outside the scope of his authority. Plaintiff argues that Newell was not authorized to borrow funds from the dealers for them. However, it is already established that the transfers in questions were made to the plaintiff's account and were not a loan made

from the dealers to the agent. Newell's decisions were terribly unfortunate and he may have failed to inform plaintiff of the risks created in the transactions, but his broad authority continued, and plaintiff, in the face of bank statements and other information, did not halt the transactions until May, 1981. Therefore, the dealers are entitled to look to plaintiff for payment of the debit amounts remaining in the plaintiff's accounts with them.

It is unfortunate that the plaintiff -- and I do not mean to make light of this -- is in the business of faith and belief and placed such unbridled faith and belief in its agent Newell, that it now suffers the consequence of his acts.

To describe these events under the rules of agency, Newell was a fully disclosed agent acting on behalf of the plaintiff, the principal. The plaintiff held out Newell as its agent to the four dealer-defendants. Even if Newell breached his fiduciary duty to the plaintiff and acted outside his actual authority, he acted with lingering apparent authority. The general rule of law is that one who has dealt with an agent in matters within the scope of his authority has the right to assume, if not informed otherwise, that such authority continues. Unless notice is given to the third party -- and none was given here until May, 1981 -- the principal is bound by the agent's acts, even though actual authority may have terminated here.

Plaintiff disputes the amount owed by arguing that such amounts must be calculated by subtracting the unsolicited loans for which the plaintiff contends it cannot be held liable. This Court has determined, however, that the transfers were not loans and are not to be subtracted from the account. Unless plaintiff has other disputes as yet unraised concerning the amounts owed, the dealers' calculations will stand as correctly reflecting the close out losses.

One other issue remains before the Court. The plaintiff previously moved for partial summary judgment on Count VII of the complaint against Bankers Trust for conversion of United States Treasury Bonds worth 1.7 million dollars. Bankers Trust

alleged that the bonds were being held as collateral for monies owed by plaintiff.

By agreement, the coupon interest has been paid by Bankers Trust to the plaintiff. As the case is postured after the September 21, 1984 ruling, the plaintiff acknowledges that it cannot at this time claim sole ownership in the bonds. Therefore, plaintiff proposes that summary judgment be entered in its favor and the bonds be sold and the proceeds distributed pro rata among the defendants. The Court declines to follow this proposal. It has now been determined that plaintiff owes Bankers Trust monies; and the balance remaining on the bonds, after satisfaction of that amount, will be returned to plaintiff.

That is the holding here. Unfortunately for the plaintiff, it is consistent with my prior rulings; and even though there is more than a pinch of sadness in the result -- and I know Mr. Ward, you are not looking for my sympathy -- it is engendered by the posture that I think your client finds itself in. Distressing though it may be, the law compels the result I have decreed here and I am obligated to find that way.

MR. WARD: Your Honor, is it the Court's view that this now concludes things in this Court?

THE COURT: I think it pretty much does; does it not? I do not know if we have anything left at all, do we?

MR. SUTHERLAND: There are two little items of Newell and Bianchina, who have not moved to be dismissed, but who -- under your Honor's previous ruling -- said there was no securities count against them, would be dismissed on those counts if they so moved. But there are those two kind of pending items.

THE COURT: Well, I think you better thank about that, Mr. Ward.

MR. WARD: Also, we asked the Court some weeks ago to give some kind of -- either a ruling or an advisory ruling, at least -- on the situation with Touche, Ross. What the Court did in that case was to say that since it had dismissed the securities fraud

count, there was no jurisdiction over Touche, Ross, since it declined to keep the pendent counts here.

On the strength of that determination, we filed over in state court against Touche, Ross, who then raised the defense in the state court that Touche, Ross was still here.

We would again urge the Court to indicate whether they are or they aren't. We think --

THE COURT: I think it is clear that Touche, Ross is not here. What I think I was asked to do was go past that, not only to say that they are not here, but what was the effect of my ruling on Touche, Ross and your ability to move against them in state court. Is that not what you wanted me to do?

MR. WARD: No. It was not our understanding --

THE COURT: You represent Touche, Ross, right?

MR. FORTI: Yes, your Honor.

I think your order -- your most recent order -- resolved the issue that was filed by the plaintiff, and it is clear that you declined to enter the judgment as final. Therefore, we are in the same posture as we were as of the September 21st ruling --

THE COURT: Well --

MR. FORTI:—that no final judgment has been entered as to the dismissal of the pendent state claims and no final judgment has been entered as to the grant of summary judgment in favor of Touche, Ross.

THE COURT: Well, that may have been true in terms of the fact that the case was pending here. I did not want to preclude your ability to go ahead, and apparently the hang up is the finality of the judgment.

I think with this ruling today we have disposed of, other than the two defendants counsel alluded to, all of the issues between the dealer-defendants and Touche, Ross; and in that posture, I think it would be advisable -- I am talking out loud here -- but to

render final the judgments now made as to the present defendants -- present who are before me -- and then whatever effect that has, it has. But I would like to know what we are going to do now with Newell and -- who was the other one?

MR. WARD: Bianchina.

MR. SUTHERLAND: Bianchina.

THE COURT: All right. I think you have to tell me that to wrap it up, I think, as completely as we can; but I think virtually all of the issues against the defendants who keep appearing before me have now been disposed of, and I really see no reason, as I sit here, why I should not make final all of the judgments that I have entered previously and the ones that I entered here today.

MR. WARD: Would you give us a few weeks -- or a few days -- for us to advise the Court what we think ought to be done with Bianchina and Newell?

THE COURT: Sure.

Is there anyone who would object for me to now say that the judgments in this case as to the prior rulings I have made, why they should not be final?

MR. SUTHERLAND: No, we would request that, your Honor.

MR. EVEN: I think so—

THE COURT REPORTER: Do you want to state your name?

MR. EVEN: Francis Even for Briggs, Schaedle. I am local.

THE COURT: All right. I do not want there to be any impediments here to your ability to prosecute the case in state court, so I am going to determine that all of the judgments now are final. I think we have disposed of everything that we need to dispose of, with the exception of the two defendants who were not movants in any motions.

So, I do not know what your pleasure is against them, but I will give you whatever time you want as to them.

MR. WARD: I should think a week would be enough. It is just a question of making a few phone calls and checking a few things. I think Newell was in bankruptcy -- went through bankruptcy.

THE COURT: Oh, he did?

MR. WARD: Yes, in California.

THE COURT: What about the other fellow?

MR. WARD: Bianchina was a very minor player -- if the depositions are to be believed -- and an exceedingly minor player. He was a partner of Newell's, but --

THE COURT: All right. I think the answer almost suggests itself, but I will give you a week to firm that up.

MR. WARD: Fine.

THE COURT: Okay?

MR. SUTHERLAND: Thank you very much, your Honor.

MR. WARD: Thank you, your Honor.

* * *

I certify that the foregoing is a correct transcript from the record of proceedings in the above-entitled matter.

Attest:

/s/ Joene Hanhardt,
Official Court Reporter

May 3, 1985

APPENDIX E

CONGREGATION OF THE PASSION,
HOLY CROSS PROVINCE,
Plaintiff-Appellant,

v.

KIDDER PEABODY & CO., INC.,
Bankers Trust Company, and
Touche Ross & Co.,
Defendants-Appellees.

No. 85-2427

UNITED STATES COURT OF APPEALS,

Seventh Circuit

Argued April 1, 1986—
Decided September 4, 1986

[Reported at 800 F.2d 177 (7th Cir. 1986)]

Before CUMMINGS, *Chief Judge*, FLAUM and RIPPLE, *Circuit Judges.*

Ripple, *Circuit Judge.* This appeal presents three issues. First, whether the appellees, Kidder Peabody & Co., Inc. (Kidder Peabody) and Bankers Trust Company (Bankers Trust), violated section 10(b) of the Securities Exchange Act of 1934 (SEA), 15 U.S.C. § 78j(b), and Securities Exchange Commission (Commission) Rule 10b-5, 17 C.F.R. § 240.10b-5. Second, whether Kidder Peabody, Bankers Trust or Touche Ross & Co. (Touche Ross) aided and abetted in any violation of the statute and the Rule. Third, whether the Congregation of the Passion, Holy Cross Province, (Congregation) is liable for the debt which remained in the accounts maintained on its behalf by Bankers Trust and

Kidder Peabody. The district court granted the motions of Kidder Peabody, Bankers Trust and Touche Ross for summary judgment on the securities law violations. It further declined to exercise pendent jurisdiction over the remaining state claims against Touche Ross and dismissed those claims without prejudice. Several months later, it granted summary judgment in favor of Kidder Peabody and Bankers Trust on their counterclaims. We affirm the judgment of the district court.

I

FACTS

The Congregation is a Roman Catholic religious community consisting of priests, brothers and students. To provide for the education of members of the community, the Congregation maintained a "Permanent" fund. The Congregation also established a "Retirement" fund to provide for older members of the community. In 1975, the treasurer of the Congregation, Father Parsons, decided that an investment advisor should manage these funds. While investigating candidates to fill that position, Father Parsons received several excellent letters of recommendation about Cranford Newell. Father Parsons invited Mr. Newell to make a presentation to the Congregation's Provincial Council. With the approval of the Council, on July 28, 1975, the Congregation hired Mr. Newell as the investment manager of its "Retirement" fund. The Congregation gave Mr. Newell "full discretion to develop and implement a prudent portfolio strategy" for investment of the million dollar fund.[1] R.309, First Boston Ex. 2. Shortly thereafter,

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[1]The Congregation of the Passion, Holy Cross Province, adopted an "Investment Philosophy and Policy." R.309, First Boston Ex. 3. The policy established an objective of a twelve to fifteen percent per annum return on the investment. In order to achieve this goal, the policy recommended that "[t]he Manager or Managers, should have a full understanding of our Investment Policy, our objectives and our expectations. Within these limits, once engaged, he should be allowed full discretionary authority and responsibility in managing the funds committed

the Congregation also entrusted Mr. Newell with a million dollars from the "Permanent" fund.

Mr. Newell selected a course of investment which included a series of arbitrage transactions.[2] In a letter addressed "To whom it may concern," Father Parsons confirmed Mr. Newell's authority "on a fully discretionary basis, to effect arbitrage transactions (involving 'long' and 'short' positions in fixed income securities) for the accounts of the CONGREGATION OF THE PASSION, HOLY CROSS PROVINCE." R.309, Kidder Ex. 3. The letter also requested and authorized dealers to accept and execute orders placed on behalf of the Congregation by Mr. Newell. *Id.* Mr. Newell used this authority to make all the investment transactions with the funds entrusted to him by the Congregation. On behalf of the Congregation, Mr. Newell placed orders with over thirty dealers. He would direct the dealer to execute a purchase or sale of a security for the Congregation's account. The dealers never offered Mr. Newell or the Congregation any investment advice. The dealers executed the transactions in accordance with Mr. Newell's instructions. A confirmation slip was sent to Mr. Newell, the Congregation and the Congregation's bank, United California Bank (Bank). The confirmation slip indicated: the transaction number; a trade date; the name of the customer; a description of the security involved; a description of the transaction; the quantity of the security involved; the price; the principal; the interest; and the net amount due. When a transaction earned a profit, the dealers would wire money to the Bank and when a transaction lost money, the Bank would wire funds to the dealers. Other than the confirmation slips, the dealer had no contact with the Congregation. When Sister Flaherty, who was tracking the

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to him." *Id.* at 4. The policy makes it clear that the manager would have full discretion over investment decisions.

[2]Arbitrage has been defined as "[t]he simultaneous purchase in one market and sale in another of a security or commodity in hope of making a profit on price differences in the different markets." Black's Law Dictionary 95 (5th ed. 1979).

transactions for the Congregation, had a question, she called Mr. Newell, not the dealers.

As early as 1976, members of the Business Advisory Board of the Holy Cross Province (Board) expressed some concern not only about the high risk involved in the arbitrage transactions but also about the pressure that the high expectations of return placed on Mr. Newell. R.309, First Boston Exs. 20, 22, 315, 316, 318, 323. The Board solicited a study of Mr. Newell's investments. An independent firm concluded that Mr. Newell had taken substantial risks in a period of uncertainty in the bond market. R.309, First Boston Ex. 223.

It was Touche Ross, the Congregation's accounting firm, which ultimately uncovered the extent of the risks Mr. Newell had taken. Beginning in 1973, the Congregation hired Touche Ross to prepare an annual report based on a review of unaudited financial statements. While preparing the 1976 report, Touche Ross consulted with the Congregation and decided to report the arbitrage investments on a cost basis. Each year, a footnote appeared in the report indicating that the arbitrage investments were not reported at current market value; instead, "[o]nly the required margin payments were carried as investments." This accounting method made Mr. Newell's investments appear profitable.

While preparing the 1980 report, however, Touche Ross began to question the location of the $3.6 million balance reported by Mr. Newell. Further investigation revealed that the actual market value of the accounts was $2.4 million less than Mr. Newell had reported. Touche Ross disclosed this information to the Congregation in February 1981. Despite this information and the Board's concerns, the Congregation transferred, in April 1981, another $500,000 to Mr. Newell. Finally, on May 6, 1981, the Congregation revoked Mr. Newell's authority to invest its funds and instructed the dealers to close all remaining accounts. By this time, Mr. Newell's investment program had not only completely depleted the $2.5 million entrusted to him but also created large debts in the accounts maintained by the dealers.

The Congregation filed suit against Mr. Newell, several dealers (including Kidder Peabody and Bankers Trust) and Touche Ross. The complaint alleged that Mr. Newell and the dealers had violated section 10(b) of the SEA, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5. The Congregation also alleged that the dealers and Touche Ross aided and abetted in these violations. Finally, the complaint contained pendent counts alleging common law breach of fiduciary duty, conversion and breach of contract. The dealers responded with counterclaims for the unpaid deficit remaining in the Congregation's accounts.

The district court granted Bankers Trust, Kidder Peabody and Touche Ross' motions for summary judgment. R.314. The court found that the dealers made no material misrepresentations and owed the Congregation no duty to disclose any information. The district court also found that this court's holding in *O'Brien v. Continental Illinois National Bank and Trust Company*, 593 F.2d 54, 60 (7th Cir. 1979), precluded a finding of primary liability under the securities laws since Mr. Newell had full discretion to develop and implement the Congregation's investment policy. R.315 at 7. Therefore, these defendants had not violated section 10(b) and Rule 10b-5. The district court also concluded that, because there was no primary violation of the statute or the Rule, these defendants could not have aided or abetted such a violation. Accordingly, the district court dismissed the securities counts against Kidder Peabody, Bankers Trust and Touche Ross and it refused to exercise pendent jurisdiction over the remaining counts. The district court also found that, because Mr. Newell had full discretion to act as the Congregation's agent in arbitration transactions and because the plaintiff had knowledge of the types of transactions Mr. Newell entered into on its behalf, the dealers were entitled to look to the Congregation for payment of the debt remaining in the accounts. Accordingly, the district court granted the dealers' motion for summary judgment on their counterclaims. R.347. Finding no just reason for delay, the district court entered final judgment in favor of Kidder Peabody, Bankers Trust and Touche Ross on all issues in both the complaint and the

counterclaims.[3] The Congregation has appealed the district court's decisions.

II

PRIMARY VIOLATION

The first issue the Congregation raises on appeal is whether Kidder Peabody or Bankers Trust violated section 10(b) of the SEA, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5. Section 10(b) makes it unlawful for any person to use "any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe" in connection with the purchase or sale of any security. Pursuant to section 10(b), the Commission promulgated Rule 10b-5 which makes it unlawful:

> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5. Although neither the statute nor the Rule expressly creates a private cause of action, the Supreme Court has noted that "a private cause of action for violation of the statute and the Rule is now well established." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 196 (1976). The Congregation alleged

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[3]When the district court granted the appellees' motions for summary judgment, *see* Fed. R. Civ. P. 54(b), several other defendants remained in the case including: Mr. Newell, Newell Associates and Richard Bianchina, one of Mr. Newell's associates.

that the dealers made misrepresentations and failed to disclose material facts in violation of section 10(b) and Rule 10b-5. For the reasons set forth in the following subsections, we affirm the district court's determination that the dealers did not violate either the statute or the Rule.

a) Fraud in the Purchase or Sale of Security

Section 10(b) and Rule 10b-5 are directed at fraud "in connection with the purchase or sale" of securities. 17 C.F.R. § 240.10b-5. *See Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 733 (1975). Therefore, the dealers submit that their conduct cannot be a violation of section 10(b) and Rule 10b-5 unless it was a misrepresentation or nondisclosure which was made to participants in a securities transaction. As this court noted in *O'Brien v. Continental Illinois National Bank and Trust Company*, 593 F.2d 54, 60 (7th Cir. 1979):

> [T]he relevant inquiry is whether plaintiffs were denied information that would or might have been useful to them in deciding whether to purchase or sell securities which they actually did purchase or sell.
>
> The important point for our analysis is the decision to which the nondisclosure related. If that decision is whether to purchase or sell a security, the nondisclosure is in connection with the purchase or sale.

In *O'Brien*, we refused to extend the implied cause of action under Rule 10b-5 to a "claim made by persons who have deliberately chosen to delegate the power to make investment decisions that the recipient of the power has misused it." *Id.* at 61. Similarly, in this case, we cannot imply a violation of section 10(b) and Rule 10b-5 when the plaintiff transferred to Mr. Newell full authority to make investment decisions. The Congregation made no investment decisions; it hired Mr. Newell for that purpose. Mr. Newell had "full discretion to develop and implement a prudent portfolio strategy." R.309, First Boston Ex. 2. Unlike the plaintiffs in *Norris v. Wirtz*, 719 F.2d 256, 259-61 (7th Cir. 1983), and *Goodman v. Epstein*, 582 F.2d 388, 412-14

(7th Cir. 1978), the Congregation was not required to approve each transaction.

The Congregation did retain the authority to increase or decrease the investment fund and ultimately to dismiss Mr. Newell. However, this authority relates to its relationship with Mr. Newell, not to any particular decision to purchase or sell a security. The federal protection of section 10(b) and Rule 10b-5 does not govern this relationship. Such an extension of federal regulation, especially in the absence of a clear congressional mandate, "would overlap and quite possibly interfere" with traditional state common law governance of such fiduciary relationships. *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 479 (1977). As we said in *O'Brien*:

> The decision to which the nondisclosure related was whether plaintiffs should terminate the trust or agency agreements or, perhaps, take some action against Continental. As Judge Flaum correctly stated in his memorandum of decision granting the motions to dismiss the federal claims,
>
> > [T]here was no investment decision to be made by plaintiffs and no such decisions were affected by any lack of information on plaintiffs' part. The "market transactions" were pure; the trust relationships allegedly were not. Rule 10b-5, however, protects the former and not the latter.
>
> 593 F.2d at 60.

b) *Misrepresentations*

Even if the alleged misrepresentations and nondisclosures occurred "in connection with the purchase or sale of any security," 17 C.F.R. § 240.10b-5, the dealers are entitled to summary judgment. There simply were no misrepresentations made by the defendants to the Congregation.

The Congregation quite candidly admits that "[t]he only contact ever made by any dealer with the plaintiff was in the form of what purported to be confirmations of purchases and sales."

Appellant's Br. at 41. However, it argues that these confirmation slips, mailed with each transaction, constituted misrepresentations. The Congregation has not, however, identified any inaccuracies in the information contained in these slips. Rather, it argues that the slips were misleading material misrepresentations because the Congregation's members lacked the sophistication to understand the confirmations. The record casts substantial doubt on the accuracy of that self-characterization by the plaintiff. [4] However, even assuming lack of sophistication on the part of the plaintiff, that fact alone would be insufficient to impose liability on the brokers. The mere fact that the plaintiff was confused does not establish the scienter element of a 10b-5 violation. *Warren v. Reserve Fund, Inc.*, 728 F.2d 741, 745 (5th Cir. 1984). Liability for this type of alleged misrepresentation, confusing confirmation slips, will only be imposed if the dealers had a special duty to ensure that the customer understood the information. Here, as we discuss more elaborately in the following subsection, the record affirmatively, and indisputably, negates a "long and dependent relationship" between the Congregation and the dealers which would create "a special circumstance that results in an obligation exceeding the normal duties owing to a casual customer or a customer whose reliance is not clearly placed with the broker-dealer. . . ." *Cant v. A.G. Beck & Co.*, 374 F. Supp. 36, 46 (N.D. Ill. 1974).

c) Duty to Disclose

Liability under section 10(b) and Rule 10b-5 for failure to disclose depends upon the existence of a duty to disclose. *Chiarella v. United States*, 445 U.S. 222, 230 (1980). This duty

---

[4]While it is not necessary to our decision, we note that there is at least some evidence to indicate that the Congregation could follow the transactions. Sister Flaherty testified that she never made an entry on the ledger unless she was satisfied that confirmation tickets agreed with cash reports from the United California Bank. Dep. Tr. at 169-70. In addition, the Congregation's Business Advisory Board and an outside firm carefully examined Mr. Newell's investments.

arises out of a relationship of trust and confidence between parties to a transaction. *Id.* Under some circumstances, a broker or dealer will have a fiduciary duty to a particular customer. That duty, however, is not based merely on one's status as a dealer. *Moss v. Morgan Stanley Inc.*, 719 F.2d 5, 15 (2d Cir. 1983). A fiduciary relationship arises only when the dealings between the customer and the dealer presuppose a special trust or confidence. Whether or not a fiduciary relationship exists between the dealer and the customer is a question of fact. *Fey v. Walston & Co.*, 493 F.2d 1036, 1049 (7th Cir. 1974); *Avern Trust v. Clarke*, 415 F.2d 1238, 1242 (7th Cir. 1969).

The Congregation argues that the dealers had a duty to disclose all relevant information, including a duty to inform the customer that its investment advisor was engaging in transactions involving greater risks that a religious organization should accept. The Congregation has alleged that a relationship giving rise to the duty to disclose exists in this case. However, conclusory statements unsupported by specific facts are not sufficient to create a genuine issue of material fact necessary to avoid summary judgment. *First Commodity Traders v. Heinold Commodities*, 766 F.2d 1007, 1011 (7th Cir. 1985).

There is no evidence in the record that the dealers and the Congregation had a special relationship of trust or confidence which would give rise to a duty to disclose. The district court correctly determined that there is no dispute on this record; the Congregation neither sought nor received advice of any kind from the dealers. Indeed, there were no contacts of any kind between the dealers and the Congregation other than the accurate confirmation slips. The dealers never recommended Mr. Newell or reassured the plaintiff about his performance. R.314 and 4. In short, the dealers acted merely as the instrument for executing the transactions orchestrated by Mr. Newell. This relationship did not create a duty to disclose, *see Affiliated Ute Citizens v. United*

States, 406 U.S. 128, 152 (1972), or a duty to make sure that the customer understood the confirmations. [5]

The dealers had no duty to disclose information and any failure to disclose did not affect an investment decision. Therefore, the dealers did not violate section 10(b) or Rule 10b-5. Accordingly, the district court correctly granted the dealers' motions for summary judgment on those counts.

III

AIDING AND ABETTING

The Congregation also contends that the defendants aided and abetted a violation of section 10(b) and Rule 10b-5. The district judge, in granting summary judgment for the defendants, held that, since there was no primary violation, there could be no aiding and abetting violation. The district judge further held that, even if a primary violation had occurred, there would be, on the uncontroverted facts before him, no liability for aiding and abetting. The broker dealers had merely executed transactions for Mr. Newell. "Even if Newell's conduct was fraudulent, there is no evidence to support the notion that the moving defendants aided and abetted that fraud." R.315 at 8. With respect to Touche Ross, the district court likewise concluded that there was "no evidentiary basis," *id.*, upon which to premise a securities fraud violation.

---

[5] A violation of section 10(b), 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5, requires an element of scienter. Negligence is not sufficient, *Ernst & Ernst v. Hockfelder*, 425 U.S. 185, 193 (1976). At least reckless behavior is required to establish liability under Rule 10b-5. *Sundstrand Corp. v. Sun Chemical Corp.* 553 F.2d 1033, 1044 (7th Cir. 1977). Although the district court did not address the issue, there is no evidence in the record to suggest that the dealers' behavior was reckless or intentional.

We have frankly acknowledged that, in light of recent Supreme Court cases,[6] there is some ambiguity about the existence of a civil cause of action for aiding and abetting a section 10(b) and Rule 10b-5 violation.[7] This court has nevertheless held that such a cause of action may be maintained under certain circumstances. *Barker v. Henderson, Franklin, Starnes & Holt*, 797 F.2d 490 (7th Cir. 1986). We have not, however, had occasion to delineate, in any comprehensive way, the elements of such a cause of action. We need not confront that question today since, under any theory of liability, the district court's judgment must be affirmed. As we have already held, the dealers did not violate the statute or the Rule. Our prior discussion of this court's holding in *O'Brien* also makes it clear that Mr. Newell did not violate section 10(b) or Rule 10b-5. Therefore, there can be no aiding and abetting violation. Moreover, the district court was quite correct in its conclusion that there is no evidentiary basis in this record for concluding that the dealers did anything more than execute brokerage transactions at the direction of the Congregation's agent, Mr. Newell. There is no factual basis from which a trier of fact could conclude that the dealers knowingly or even recklessly furthered any fraudulent scheme. Nor, in the absence of any independent affirmative duty, can their silence be the basis of such liability. Similarly, the district court was correct in its conclusion that there was no such basis for liability against Touche Ross.

IV

PENDENT CLAIMS

The only remaining counts against the appellees were pendent common law counts. The district court, after properly granting judgment for the defendants on the federal securities

---

[6] *See Ernst & Ernst*, 425 U.S. at 191 n.7; *see also Herman & Maclean v. Huddleston*, 459 U.S. 375, 379 n.5 (1983).

[7] *See SEC v. Holschuh*, 694 F.2d 130, 140 n.15 (7th Cir. 1982); *Sundstrand Corp.*, 553 F.2d at 1044 n.15.

fraud counts, did not abuse its discretion by refusing to exercise pendent jurisdiction over the remaining counts. We affirm the district court's decision to grant the defendants' motion for summary judgment.

V

COUNTERCLAIMS

The Congregation also appeals the district court's decision to grant the dealers' motion for summary judgment on their counterclaims. It argues that Mr. Newell lacked the authority to enter into the type of transactions which created the debts in the Congregation's accounts. The Congregation claims that the risk involved in the type of arbitrage transactions Mr. Newell undertook far exceeded the risk of those authorized. It characterizes the transactions between the dealers and Mr. Newell as unauthorized loans for which it is not responsible. The record does not support the Congregation's arguments. The record reveals that the Congregation gave Mr. Newell the authority to enter into arbitrage transactions. That authority placed no restriction on the type of arbitrage transactions. Moreover, the record affirmatively shows that the Congregation and its Business Advisory Board were aware of the types of transactions involved and were concerned about the risks associated with these transactions. When it became apparent that the investments were not good risks, rather than revoking Mr. Newell's authority, the Congregation entrusted him with another $500,000 to cover his investments.

The Congregation granted Mr. Newell full authority to enter into these transactions; it was fully aware of the transactions and the type of risks involved. It must now be responsible for the deficit created when the investments lost money. No genuine issue of material fact remains unresolved. Therefore, the dealers are entitled to summary judgment on their counterclaims.[8]

---

[8]On appeal, the Congregation has also argued that there is a discrepancy between the dealers' accounts and the Congregation's records. The district court gave the Congregation the opportunity to object to the amount owed. To that point it had not raised an objection other than the

VI

CONCLUSION

The district court correctly concluded that, as a matter of law, none of the defendants could be found to have violated section 10(b) or Rule 10b-5. Nor could they be found to have aided and abetted such a violation. Therefore, it properly granted summary judgment for the defendants. The record on summary judgment also establishes, as a matter of law, that the Congregation authorized and was aware of the type of transactions which created the debts in the accounts maintained with the dealers. Therefore, the district court properly granted the dealers' motion for summary judgment on their counterclaims. Accordingly, the judgment of the district court is affirmed.

AFFIRMED.

---

characterization of the transactions as loans. The district court, therefore, accepted the dealers' calculations as correctly reflecting the close out losses. R.347 at 8. We will not consider an objection not raised in the district court.

APPENDIX F

ILLINOIS SUPREME COURT
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May 27, 1994

Mr. John J. Verscaj
Bell, Boyd & Lloyd
Three First National Plaza
Chicago, IL 60602

No. 73224—Congregation of the Passion, Holy Cross Province, etc., appellee, v. Touche Ross & Co., appellant. Appeal, Appellate Court, First District.

The Supreme Court today DENIED the petition for rehearing in the above entitled cause.

Nickels, J., took no part.

The mandate of this Court will issue to the appropriate Appellate Court and/or Circuit Court or other agency on June 6, 1994.

APPENDIX G

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Article I, § 8, cl. 18 of the Constitution of the United States provides, in part, that Congress shall have the power:

> To make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof.

Article III, § 1 of the Constitution of the United States provides, in part:

> The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish.

Article III, § 2, cl. 1 of the Constitution of the United States provides:

> The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority;—to all Cases affecting Ambassadors, other public Ministers and Consuls;—to all Cases of admiralty and maritime Jurisdiction;—to Controversies to which the United States shall be a Party;—to Controversies between two or more States;—between citizens of different States;—between citizens of the same State claiming Lands under Grants of different States.

Article VI, cl. 2 of the Constitution of the United States provides:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in

the Constitution or Laws of any State to the Contrary notwithstanding.

Section 5/2-1303 of the Code of Civil Procedure of Illinois, 735 ILCS 5/2-1303 provides:

> Interest on judgment. Judgments recovered in any court shall draw interest at the rate of 9% per annum from the date of the judgment until satisfied or 6% per annum when the judgment debtor is a unit of local government, as defined in Section 1 of Article VII of the Constitution, a school district, a community college district, or any other governmental entity. When judgment is entered upon any award, report or verdict, interest shall be computed at the above rate, from the time when made or rendered to the time of entering judgment upon the same, and included in the judgment. Interest shall be computed and charged only on the unsatisfied portion of the judgment as it exists from time to time. The judgment debtor may be tender of payment of judgment, costs and interest accrued to the date of tender, stop the further accrual of interest on such judgment notwithstanding the prosecution of an appeal, or other steps to reverse, vacate or modify judgment.

SEP 27 1994
OFFICE OF THE CLERK

No. 94-341

In The

Supreme Court of the United States

October Term, 1994

TOUCHE ROSS & CO.,

Petitioner,

v.

CONGREGATION OF THE PASSION,
HOLY CROSS PROVINCE,

Respondent.

On Petition For A Writ Of Certiorari To The Illinois Supreme Court

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

THOMAS P. WARD
(*Counsel of Record*)
McBRIDE, BAKER & COLES
500 West Madison Street
Chicago, Illinois 60606
(312) 715-5700

DAVID C. GUSTMAN
THOMAS KOTTLER
FREEBORN & PETERS
311 South Wacker Drive
Suite 3000
Chicago, Illinois 60606
(312) 360-6000

Attorneys for Respondent, Congregation of the Passion, Holy Cross Province

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
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QUESTIONS PRESENTED

(1) Whether a writ of certiorari may be granted where the alleged federal questions are raised for the first time in the United States Supreme Court, were never "pressed" by petitioner in the state's highest court and were never "passed upon" by the state's highest court?

(2) Whether certiorari may be granted based upon the claim that the state's highest court failed to apply federal common law where the petitioner took a different position in the state's highest court and requested that it apply the state's substantive law and not federal common law?

(3) Whether a reviewable issue is raised by petitioner's assertion that a state's highest court erred by applying its own law on the issue of the collateral estoppel effect to be given to a prior federal adjudication, when the law applied by the state's highest court is the same as the federal common law?

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JURISDICTION

Petitioner has correctly stated the grounds on which it seeks to invoke the jurisdiction of the Supreme Court. Respondent asserts the Court lacks jurisdiction to grant the requested writ since the constitutional issues raised in the Petition were not "pressed or passed upon below." *Webb v. Webb*, 451 U.S. 437, 4 39 (1981).

STATEMENT OF THE CASE

This case presents the Court with a unique set of factual and procedural circumstances. The uncommon nature of these circumstances, as discussed below, make this case unsuitable for certiorari review as they take the case out of the commonplace and present the Court with issues devoid of common appeal or application.

This Petition arises from a state court case which alleged accounting malpractice and breach of contract under Illinois common law. Following a four week jury trial in the Circuit Court of Cook County in 1988, the jury rendered a verdict in favor of the plaintiff, Congregation of the Passion, Holy Cross Province ("the Congregation")[1] and against its former independent accounting firm Touche Ross & Co. ("Touche Ross") finding it liable

[1] The Congregation of the Passion, Holy Cross Province, is an Illinois not-for-profit corporation with no parent or subsidiary corporations. The priests and brothers who comprise the Congregation are members of the Passionists, an order of the Roman Catholic Church. Touche Ross has correctly stated its status in the Petition for Certiorari.

for accounting malpractice/negligence and breach of contract. A count alleging breach of fiduciary duty was dismissed by a directed verdict. Judgment was entered in the amount of $3,819,352, plus costs.

The claims against Touche Ross involved malpractice – spanning a five year period – relating to the values Touche Ross reported to the Congregation of U.S. Government Bonds, purchased for the Congregation by a San Francisco investment adviser, Cranford D. Newell ("Newell"). Initially, the Congregation filed suit in federal court against Newell and four bond dealers alleging violations of Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934. Touche Ross was alleged to have aided and abetted Newell and the bond dealers' 1934 Act violations, and the Congregation also asserted pendant common law claims for accounting malpractice and breach of contract. On motions for summary judgment on the federal security law claims only, the federal district court held that the Congregation could not prove a Rule 10b-5 violation against the dealers or Newell. There being no primary securities law violation, an aiding and abetting claim against Touche Ross could not survive. (App. C-4,5).[2]

Touche Ross thereupon requested the district court to dismiss *without prejudice* the pendant state laws claims against it, the district court did so, and the Congregation re-filed those claims in the Circuit Court of Cook County.

---

[2] For the purpose of consistency, the Congregation will use the same references to trial exhibits, the Report of Proceedings and the record on appeal that were used by Touche Ross in its Petition. References to documents appended to the Petition for Certiorari will be to "App. ___-___."

None of these claims (i.e., accounting malpractice/negligence, breach of contract and breach of fiduciary duty) had been litigated, considered, or ruled upon by the federal courts.

In a motion to dismiss filed in state court, Touche Ross argued that the prior federal litigation acted to preclude the Congregation from relitigating specific factual issues which it claimed created an insurmountable defense, on the basis of *Illinois* collateral estoppel principles. The trial court denied the motion to dismiss and a subsequent summary judgment motion, a directed verdict motion and post-trial motions, all asserting that Illinois substantive collateral estoppel principles prevented the Congregation from pursuing its common law claims against Touche Ross. Touche Ross then appealed to the Illinois Appellate Court on a variety of grounds, including assigning as error the trial court's failure to give collateral estoppel preclusionary effect to certain alleged factual "findings" of the federal courts. However, Touche Ross did not raise any constitutional issues in the Illinois trial or Appellate Court, and urged the Appellate Court to employ the *substantive law of Illinois* relating to the application of collateral estoppel. (Ill. App. Ct. Brief filed Aug. 28, 1989 at p. 27).

At both appellate levels, Touche Ross failed to raise any constitutional issues, and argued that the application of the collateral estoppel argument was governed *by the law of Illinois*. (*Id.*; Ill. Sup. Ct. Brief filed May 5, 1992, at p. 39, f.n. no. 20). In the Illinois Supreme Court, though failing to raise *any* constitutional issue regarding collateral estoppel, Touche Ross did make an argument relevant but contrary to its position as stated in its Petition.

Touche Ross urged the Illinois Supreme Court *not to reach any United States constitutional implications raised by its collateral estoppel arguments and to rely solely on Illinois law to determine whether the prior federal decisions collaterally estopped the Congregation from pursuing its state law claims against Touche Ross.* As Touche Ross stated in its opening brief in the Illinois Supreme Court:

> The issue here is ultimately of constitutional dimension for the constitutional judicial power of the United States, the necessary and proper clause and the Supremacy Clause require that state courts give full faith and credit to the judgments of the federal courts and this extends to the collateral estoppel effects of those judgments . . . *But the constitutional issues need not be reached since the proper legal principle is found in Illinois law itself and requires reversal of the judgment below.*

Ill. Sup. Ct. Brief Filed May 5, 1992, at p. 39, n. 20 (emphasis added).

The Petition filed in this Court marks the first time Touche Ross has asserted that *any* constitutional issues related to collateral estoppel should be considered by *any* tribunal. Moreover, before the Illinois courts Touche Ross consistently asserted that Illinois law governed the collateral estoppel issues, *not federal law.*

A. The Congregation and its Investments

The Congregation is a Roman Catholic religious order which derives its operating budget from donations and from investment income. The priests and brothers of

this religious order have no formal training or background in investments or accounting, and thus hire and rely upon outside investment specialists to manage their funds and on outside accountants to accurately report the results the fund managers achieve. (R.P. 718-19; 2643-44).

Touche Ross had, beginning in 1973, been engaged by the Congregation to conduct a review of its financial records, and to prepare its financial reports. Each year the parties mutually executed an engagement letter. Touche Ross agreed each year to determine the market value of the Congregation's investments and represented in each financial statement that it prepared for the Congregation that the Congregation's investments were reported at market value. (P.X. 3,4,5,6, 44-49 at Note A(2) (Investments)).

In 1976, Touche Ross encountered for the first time an investment portfolio of U.S. Treasury bonds managed by Newell. (R.P. 1282-83). The Congregation had committed $2.0 million to Newell's management. (R.P. 1069). The Congregation provided Touche Ross with each confirmation and statement sent by the dealers, and separate transaction statements sent by Newell – in short, everything needed to identify each security held and its market value. (R.P. 1540-41, 1696, 1702; P.X. 128M).

B. The Role of Touche Ross and its Misstatements to the Congregation

The Touche Ross accountants conducting the 1976 review established that although only $2 million had been placed under Newell's management, the face value of the bonds held or sold short at June 30, 1976 was $44.5

million. (P.X. 12). That 22:1 leverage was made possible by practices employed by government securities dealers which permitted a purchase of one bond issue to be set off against the short sale of another, passing market risk on both issues to the customer but calling for only minuscule cash transfers. (R.P. 1325-26; 1535-36). Another method for transferring market risk with virtually no cash changing hand was the repurchase agreement ("repo").

The Congregation's bookkeeper, Brother Kent, who was a member of the order, had been doing his best to record on spread sheets all of the information he was receiving on the transactions that led to the $44.5 million open positions. (R.P. 1687, 1701-05). Despite having exposure to this information, Brother Kent had no understanding of its meaning or its relevance to the value of the Congregation's investments. (R.P. 1689-96, 1701-05). Nor did Brother Kent have any idea how such positions should be reported in financial statements – he was waiting for Touche Ross to advise the Congregation on the correct way to determine the value of these investments and how such value should be reported on the statements Touche Ross had undertaken to prepare. (*Id.*)

The Touche Ross accountants appear to have been as bewildered as Brother Kent was. They told the Congregation they would discuss the issue with senior management at Touche Ross and would come back with a recommendation. (R.P. 1702-05). Touche Ross decided the method to present these investments in financial reports. (App. E-4). The method it chose led to disastrous results.

Touche Ross determined that the "investment" consisted of the amount of cash the Congregation paid at inception to settle the spread, or to put the repo in place. This advice was based on a note written in the Touche Ross 1976 work papers, which was never made known to the Congregation until produced during discovery.[3] The

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[3] That note stated:

"3) Arbitrage – when Newell determines that there is a temporary fluctuation in the price of a government security in relationship to other government securities he buys or sells short that security and purchase [sic] or sells short another government security at the same time. When the fluctuation is eliminated he reverses his previous purchase and short sale and takes a profit (or loss). These arbitrages are generally for over $1 million dollars [sic] and a small fluctuation (1/32 of 1%) can involve a substantial amount of money. The only money actually invested by the Congregation is for margin required by the dealers (typically the amount of the purchase less the amount of the short sale). The risk is minimized since only U.S. government securities are traded and the chance of default is small.

At June 30, 1976 the Congregation had open arbitrages aggregating $22.25 million at par value and short positions in the same amount. Since the trades in these securities involve minor fluctuations in price (1/32 or even 1/64 of a point) and there is no source which can tell us market value closer than 1 point ($222,500) it was decided not to gross up the balance sheet to reflect these items at market.

Instead footnote disclosure will be made of the total amounts involved and only the margin outstanding on these arbitrages will be included in investments.

W. Cornfield
10/4/76"

(PX 1; App. A-3)

effect of reporting these investments as Touche Ross decided to report them is that the Congregation would never know the market value of any bond holding in the Newell managed accounts that remained open at the end of a fiscal year. Any unrealized losses or gains occurring due to fluctuations in market prices would not be reflected in the figures which were reported in the annual financial reports prepared by Touche Ross. (App. A-3). Touche Ross believed – incorrectly as it turned out – that the values it reported were essentially equal to market values. (P.X. 78, 93, p.7; R.P. 1970, 2695-96).

The relationship of the Congregation to Newell could have been terminated at any time for any reason including that the adviser's investment decisions were causing significant losses of the investment capital under his management (R.P. 2663-66). Touche Ross was to confirm the accuracy of profit/loss figures derived from Newell's reports, including the market value of the portfolio on a yearly basis. Every engagement letter from 1976 through 1980 declared, "[i]nvestment market values will be tested by reference to published market quotations" (P.X. 3,4,5,6). No such testing was ever conducted by Touche Ross. (R.P. 1296-7; 2026-28). Due to its faulty assumptions as contained in the Cornfield note and its lack of testing, Touche Ross *overstated* the value of these investments in ever-increasing amounts from $214,000 in 1976 to $2,400,000 in the draft report sent to the Congregation in September 1980. (App. A-4,5).

The difference between reporting these investments as Touche Ross did, and at market value, as it agreed to do, was:

Fiscal Year	Value Reported By Touche Ross	Actual Market Value	Unreported Losses on Financial Stmts Prepared By Touche Ross
1976	$2,166,322	$1,951,520	($214,802)
1977	1,795,346	1,471,720	(323,626)
1978	1,792,748	319,861	(1,472,887)
1979	2,226,014	878,638	(1,347,376)
1980 (Draft)	3,706,190	1,286,410	(2,419,780)

(App.A-5,7; B-9).

The 1980 draft report showing a portfolio with $3.7 million was delivered in September. (P.X.48). The following month the engagement partner at Touche Ross asked one of the junior accountants where the $3.7 million was. No one could answer. (P.X. 94, R.P. 1840-42). Between October, 1980 and April, 1981, Touche Ross learned that the values it had been reporting on the financial statements it prepared for the Congregation were grossly overstated, but it did not so inform the Congregation until April 1981. (R.P. 2682). A final 1980 report (replacing the draft report) was dropped off at the Congregation late in April, 1981 with no explanatory letter and with no one offering to explain five years of errors. (R.P. 2747-48). Shortly after receiving the final 1980 financial report – which also restated the previously reported values of the Newell investments for the prior three years – the Congregation closed its accounts with Newell. (App.A-7; R.P. 777; P.X. 49, note H).

C. The Federal Litigation

The Congregation's federal court action against the bond dealers was based solely upon alleged violations of Section 10(b) and Rule 10b-5. The federal claim asserted against Touche Ross was for aiding and abetting those primary securities laws violations. The district court granted summary judgment in favor of the bond dealers, and the Seventh Circuit affirmed, basing its ruling on *O'Brien v. Continental Illinois Nat'l Bank & Trust Co.*, 593 F.2d 54, 60 (7th Cir. 1979). (App. C-5,6). By delegating full discretionary authority to Newell, it was held that the Congregation retained no investment decision, and that denial of information to it could not be "in connection with the purchase or sale of a security" as required by this Court in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 733 (1975). (App. E-7,8). With respect to Touche Ross, the Seventh Circuit merely found that there could be no claim against it for aiding and abetting, without a primary violation on the part of the dealers. (App. E-11,12).

The common law counts against Touche Ross were dismissed by the federal district court, *without prejudice*, and were not ruled upon. There was no occasion for either federal court to make any findings relating to the pendant claims because dismissal of the securities laws claims eliminated the basis for federal jurisdiction. In fact, Touche Ross argued successfully that the state law claims should not be considered:

> It would be inappropriate to address their merits in this forum because once a plaintiff's federal claim is dismissed, pendant state law claims should also be dismissed.

(C. 1190).

The federal district court agreed that it would not address issues other than aiding and abetting as to Touche Ross, and it did not do so. The federal district court specifically held that these issues were to be resolved by the state court:

> The only federal claim lodged against Touche, Ross is also premised on the aiding and abetting theory. My earlier discussion regarding *O'Brien* and the lack of primary violation, also precludes a finding of liability against Touche, Ross.
>
> Additionally, there is no evidentiary basis to conclude that Touche, Ross aided or abetted Newell in anything he did, let alone a securities fraud scheme.
>
> The remaining claims are all state law causes of action. Because this court is one of limited jurisdiction, and a state court could easily preside over the remaining issues, I will decline to exercise pendant jurisdiction over these matters and hereby dismiss them.

(App. C-6).

D. The State Court Trial and Appeals

After the dismissal of the common law claims, the Congregation re-filed them in state court. In the trial court, Touche Ross repeatedly sought to prevent a decision on the merits of the malpractice and breach of contract claims, asserting that alleged "findings" of the federal courts relating to the resolution of the federal claims collaterally estopped the common law claims. (C. 10348-58, 11373-416, 11780-82, 11785-86). In its various motions filed before the trial court, Touche Ross argued

the application of Illinois law to determine the collateral estoppel effect, if any, of the alleged "findings" of the federal courts. No federal constitutional issues were raised with the trial court.

The Illinois Appellate Court was next urged to give collateral estoppel effect to the purported "findings" of the federal courts. (Brief of Touche Ross filed August 28, 1989 at 25-35; Reply Brief of Touche Ross filed December 6, 1989 at 11-16.) Touche Ross failed to raise in the Appellate Court any of the constitutional issues asserted here. Again, its collateral estoppel argument in the Appellate Court rested solely on the substantive law of Illinois, and not on federal issue preclusion principles.[4] Collateral estoppel was held not to apply because no determination on the merits of the state law claims asserted by the Congregation was ever sought by Touche Ross, or was ever made by a federal court. (App. B-16,17). As the Appellate Court stated, "the first time a trier of fact ever considered evidence on the issues of proximate cause and knowledge or other factors pertaining to Touche Ross' purported negligence and breach of contract was at the trial below." (App. B-16). The Appellate Court relied on many of the state court cases cited to it by Touche Ross.

The Illinois Supreme Court next considered the refusal of the lower courts to give collateral estoppel

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[4] For example, in the first subsection of its collateral estoppel argument in its opening brief in the Appellate Court, Touche Ross stated that, "[t]he Illinois Supreme Court has held that the 'only pertinent questions' for the application of collateral estoppel are . . . " and cited to *Ballweg v. City of Springfield*, 114 Ill. 2d 107, 113, 499 N.E.2d 1373, 1375 (1986).

effect to the "findings" allegedly made by the federal courts. Touche Ross again failed to raise any of the constitutional issues raised here. Contrary to the position Touche Ross now takes, it implored the Illinois Supreme Court to avoid potential constitutional issues, and to rely solely upon the substantive law of Illinois: *"[b]ut the constitutional issues need not be reached since the proper legal principle is found in Illinois law itself and requires reversal of the judgment below."* (Ill. Sup. Ct. Brief of Touche Ross filed May 5, 1992 at 39, n.20).

Like the lower state courts, the Illinois Supreme Court correctly recognized that the prior federal opinions would, in the proper circumstances, collaterally estop common law causes of action asserted by the Congregation. The Illinois Supreme Court did not, as Touche Ross claims, "disregard a decree of a court of the United States." (Pet. at 2). Rather, the Illinois Supreme Court recognized the prior federal rulings and carefully analyzed their potential collateral estoppel effect. The court then decided that the "findings" alleged by Touche Ross to have been made by the federal courts were not sufficient to collaterally estop the Congregation from pursuing its malpractice and breach of contract claims against Touche Ross.

In so finding, the Illinois Supreme Court first held that collateral estoppel did not apply to findings made by the federal court that were not relevant to plaintiff's negligence and breach of contract claims, because factual findings as to Newell's relationship with the Congregation "have no bearing on whether [Touche Ross] is liable to [the Congregation] for the manner in which [Touche

Ross] recorded the Newell investments in [the Congregation's] financial report." (App. A-12). The Illinois Supreme Court next determined that many of the "points urged by defendant as findings *were not actually decided* in the Federal adjudication" or were "taken out of context" by Touche Ross. (App. A-12,15) (emphasis added). After careful analysis, the Illinois Supreme Court also found that certain claimed preclusive findings of the federal courts were "not necessary" to the federal decisions. (App. A-13).

For the first time, in the introduction to its Petition for Rehearing, Touche Ross suggested that there were relevant constitutional implications to the Illinois Supreme Court's failure to give collateral estoppel effect to the purported federal court findings. (Petition for Rehearing of Touche Ross filed on May 12, 1994 at 3). However, in the argument section of its Petition for Rehearing, Touche Ross failed to press any constitutional arguments, and similarly failed to urge, as it does now for the first time here, that the Illinois Supreme Court should have applied federal rather than Illinois preclusion principles. Since these issues were never properly raised before the Illinois Supreme Court, they were never ruled upon, either in its original ruling or in its denial of Touche Ross' Petition for Rehearing.

E. Misstatements of Fact in Petition

There are several material misstatements repeatedly made in the Petition which have a significant bearing on the question of what issues would properly be before the Court if certiorari were granted. Touche Ross repeatedly

claims that the federal courts found that it made no misrepresentations to the Congregation. (See Pet. at 6, 7, 14, 20, 21, 22, 27 and 28). Neither the district court nor the Seventh Circuit ever made such a finding. Touche Ross' claim that the Seventh Circuit determined that there was no evidentiary basis from which to conclude that it had made "misrepresentations" to the Congregation is pure fiction. It is true that the district court and the Seventh Circuit found the dealer defendants made no misrepresentations to the Congregation upon which a primary federal securities fraud claim could be based. (See App. C-3,5; E-8). It is equally clear from the context in which these findings were made that they relate to the dealer defendants and not to Touche Ross. Also, the federal courts never found that the Congregation did not rely upon Touche Ross or the misrepresentations contained in the reports created by it as claimed by Touche Ross. (Pet. at 23).

Touche Ross also inaccurately claims the federal court determined that a "joint decision was made" between the Congregation and Touche Ross on the method of reporting the investment in the financial statements. (Pet. at 4; See also Pet. at 21, 24, 27). No such agreement was ever found by the federal courts. Touche Ross also states that "Touche Ross had consulted with the Congregation concerning the reporting of the investments and it *was* decided to report the investments at cost" (emphasis added). (Pet. at 7; See also Pet. at 29). No such findings were ever made by the federal courts. The actual quote from which these misstatements are taken states that, "[w]hile preparing the 1976 report, Touche Ross consulted with the Congregation and decided to

report the arbitrage investments on a cost basis." (App. E-4). A natural reading of this statement suggests that Touche Ross made the reporting decision on its own. Such a conclusion makes sense in the context of the relationship between the Congregation and Touche Ross – the Congregation had hired the independent accounting firm of Touche Ross to make exactly this type of decision because the Congregation lacked the expertise to do so. Touche Ross' strained reading of this statement and its inclusion of the word "was", which is not found in the Seventh Circuit's opinion, confirms the misstatement.

Touche Ross also misstates the Seventh Circuit's opinion when its states, "the Business Advisory Board ("BAB")[5] monitored the Newell arbitrage activities, as did the Congregation's own officers." (Pet. at 4). There was no such finding made by the Seventh Circuit. The only reference on the page cited by Touche Ross for this proposition is a reference to the finding that the BAB had a consultant look at the Newell investments and that the consultant determined they were risky. The federal courts never found, as Touche Ross suggests in its Petition, that the BAB or the Congregation knew the true value of the Newell managed funds, or the extent of their losses, until Touche Ross finally informed them in 1981.

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[5] The BAB consisted of laymen who volunteered to meet when asked to do so with the Congregation's governing council. No member of the BAB had any experience with government bond dealers' trading practices.

REASONS FOR DENYING THE PETITION FOR WRIT OF CERTIORARI

There is nothing presented by this Petition that makes this case appropriate for review. *First*, by failing to raise the purported constitutional issues in the Illinois Appellate or Supreme Courts and by seeking to raise them for the first time in its Petition, Touche Ross has failed to meet the "passed and pressed upon below" rule which is an essential prerequisite to this Court's ability to grant a Petition. *Second*, since Touche Ross urged the Illinois Supreme Court to apply the substantive law of Illinois to determine the collateral estoppel effect of the prior federal adjudication, it cannot now argue that the court erred by failing to apply federal preclusion principles. *Third*, there is no federal law question raised on which any conflict has developed, either between federal circuits, among state supreme courts, or between the Illinois Supreme Court and governing Supreme Court precedent or a decision of a federal appeals court. *Fourth*, the outcome of the case below would not have been altered had the Illinois Supreme Court applied the federal common law now advocated by Touche Ross. This is so because (1) Illinois collateral estoppel law is generally more favorable to Touche Ross' position than federal law, and (2) the Illinois Supreme Court in fact applied the elements of federal common law anyway. *Fifth*, the novel and complex procedural and factual circumstances involved in this case make it inappropriate for certiorari review because any decision based upon it would lack general application. The Illinois Supreme Court's opinion rejecting collateral estoppel in the unique context presented here does not present an important issue of federal law, nor does it portend significant practical

consequences. This case simply does not present any issues of general public concern.

I. Certiorari Should Not be Granted Since the Constitutional Issues Raised in the Petition Were Not Pressed and Passed Upon Below

This is the first time Touche Ross has asserted that there are constitutional issues concerning the application of collateral estoppel principles which should be considered by any court, or that the Illinois Supreme Court erred by applying Illinois law to determine the collateral estoppel effect of the prior federal judgments. Touche Ross cannot raise these issues for the first time in this forum. The attempt to so raise these issues is made even more untenable by the fact that Touche Ross beseeched the Illinois Supreme Court to ignore any potential constitutional issues and look solely to Illinois substantive law for the proper legal principles to be applied.

The Court's certiorari jurisdiction over decisions from state courts is limited by the principle that, "[i]n reviewing the judgments of state courts under the jurisdictional grant of 28 U.S.C. § 1257, the Court has, with very rare exceptions, refused to consider petitioners' claims that were not raised or addressed below." *Yee v. City of Escondido, California*, 112 S.Ct. 1522, 1531 (1992). This restriction is known as the "pressed and passed upon below" rule. There are no valid reasons why the Court should abandon this established practice and grant certiorari here.

Early cases unequivocally held no certiorari jurisdiction existed unless a federal question had been both raised and decided in the state court below. *Crowell v.*

Randell, 35 U.S. 368 (1836); *Owings v. Norwood's Lessee*, 9 U.S. 344 (1809). More recent cases have reaffirmed the validity of these jurisdictional requirements. *Webb v. Webb*, 451 U.S. 493, 496 (1981); *Hill v. California*, 401 U.S. 797, 805-806 (1971); *Cardinale v. Louisiana*, 394 U.S. 437, 438-39 (1969). Only under extenuating circumstances has this Court held the "pressed and passed upon" rule not to be jurisdictional. *Illinois v. Gates*, 462 U.S. 213, 219 (1983) commented that "some cases have treated the so-called 'not pressed or passed upon below' rule as merely a prudential restriction." This issue, however, need not be resolved here since this Court should deny the Petition on both jurisdictional and prudential grounds.

Assuming the "pressed and passed upon below" rule is a jurisdictional requirement, it must function to preclude certiorari. Touche Ross never "pressed" the federal claims identified in the Petition during the state court appellate process, and affirmatively sought to have the Illinois Supreme Court avoid any such issues and apply Illinois collateral estoppel principles. This Court dismissed a writ of certiorari as improvidently granted where a party urged a decision based on a theory which differed from the position taken in the Court of Appeals. *Bankers Trust Co. v. Mallis*, 435 U.S. 381, 388 (1978). Touche Ross cannot have a writ granted on a theory which is the polar opposite of the theory it espoused in the courts below.

Touche Ross' reference of potential constitutional implications in the introduction to its Petition for Rehearing in the Illinois Supreme Court does not constitute "pressing" of the issue. The mere mention of constitutional provisions and their potential application, without

citation of cases and exposition of the bases for the federal claim, does not constitute "pressing" of the issue. *Webb*, 451 U.S. at 496-97 (petitioner who used the phrase "full faith and credit" in the state court proceedings, but without ever having cited cases to support a full faith and credit claim failed to raise the issue sufficiently to establish certiorari jurisdiction).

Even if Touche Ross had adequately raised the newly-minted "federal question" in its petition for rehearing, it would still be jurisdictionally insufficient unless the state court actually entertained the petition and ruled on the federal question. *Radio Station WOW, Inc. v. Johnson*, 326 U.S. 120, 128 (1945). To constitute a reviewable judgment under these circumstances, the order denying the petition for rehearing must be more than a cursory recitation that the petition has been considered and denied. *Consolidated Turnpike Co. v. Norfolk & O.V.R. Co.*, 228 U.S. 326, 333-34 (1913). There is simply no basis for Touche Ross to claim that it "pressed" any federal questions in the courts below.

It is equally clear that the Illinois Supreme Court never "passed" on the constitutional issues raised by Touche Ross in its Petition for Certiorari. The Illinois Supreme Court's order denying Touche Ross' Petition for Rehearing is silent on the constitutional issues now being asserted by Touche Ross. (App. F-1). There is no mention in any of the state court opinions, either at the trial or appellate levels, suggesting that federal constitutional issue claims were presented, considered or ruled upon. A rare exception to the "pressed and passed upon below" rule may apply where the petitioner is (1) able to show

that the decision of the state's highest court was a surprise *and* (2) demonstrate that the federal question was actually raised in the petition for rehearing but was ignored by the court. *Herndon v. Georgia*, 295 U.S. 441, 443-44 (1935). Touche Ross cannot meet either of these burdens. There is no basis for Touche Ross to argue that it took advantage of any of the many opportunities available to it to raise the federal questions now asserted. Equally, it would be fallacious for Touche Ross to argue that the Illinois Supreme Court's application of Illinois collateral estoppel law came as a surprise, since Touche Ross itself requested the application adopted by the Illinois Supreme Court.

That Touche Ross failed to raise in the Illinois state courts the issues it now seeks to be reviewed is further substantiated by its failure to comply with Supreme Court Rule 14.1(h). That Rule requires that:

> If a review of a judgment of a state court is sought, the statement of the case shall also specify the stage in the proceedings, both in the court of first instance and in the appellate courts, at which the federal questions sought to be reviewed were raised; the method or manner of raising them and the way in which they were passed upon by those courts; and such pertinent quotation of specific portions of the record or summary thereof, with specific reference to the places in the record where the matter appears . . . as will show that the federal question was timely and properly raised *so as to give this Court jurisdiction to review the judgment on a writ of certiorari* (emphasis added).

Touche Ross' statement of the case omits mention of any of the jurisdictional facts called for in Rule 14.1(h). The

reason for this omission is clear – having failed to raise the "federal questions sought to be reviewed" at any point in the state court proceedings, Touche Ross is unable to comply with this rule.

Certiorari must also be denied under the less restrictive "prudential" standard applied in a small minority of cases. Principles of comity "require that the state courts be afforded the opportunity to perform their duty, which includes responding to attacks on state authority based on the federal law, or, if the litigation is wholly private, construing and applying the applicable federal requirements." *Webb*, 451 U.S. at 499. There are also practical reasons for requiring a federal issue to have been adequately presented in the state-court system before granting certiorari. These reasons include (1) the need to develop the record necessary for Supreme Court review; (2) the desire to provide state courts with the ability to pretermit the federal issues by identifying and acting upon independent and alternate state grounds; and (3) the ability of state courts to handle a larger number of federal claims on appeal, than can the Supreme Court, as well as providing this Court with opinions that may obviate the need for plenary review. *Gates*, 462 U.S. at 221-22; *Webb*, 451 U.S. at 500-01. This case clearly falls within the parameters of the prudential restriction for denying certiorari.

II. The Petition Fails to Raise a Federal Question Worthy of the Court's Plenary Review

The fundamental premises underlying Touche Ross' Petition are that the Illinois Supreme Court's failure to apply federal collateral estoppel law created a reviewable

federal question and that applying such principles in this case would lead to a different result. Those premises are false for a variety reasons. First, there is no split in the decisions of the Circuit Courts relevant to any issue in this case. Second, there is no conflict in the decision of the Illinois Supreme Court and a United States court of appeals on a similar federal question. Third, Illinois collateral estoppel law is more advantageous to Petitioner than federal collateral estoppel law. Thus, if Touche Ross was unable to satisfy the Illinois collateral estoppel rules, federal collateral estoppel law would not mandate a different result. Even if the Court were to overlook the procedural flaws in Touche Ross' Petition, the Petition should still be denied because Touche Ross has failed to demonstrate any basis for reaching a different result on remand. The Illinois Supreme Court correctly determined that collateral estoppel did not bar the Congregation's common law negligence and breach of contract claims against Touche Ross. Touche Ross' request for relief from this Court is not based on the depravation of a vital constitutional right, but rather its failure to obtain a favorable ruling from the Illinois Supreme Court.

A. There is No Split in the Circuits Relevant to this Matter and No Clash Between the Decision of the Illinois Supreme Court and a Federal Circuit Court on a Federal Question

Touche Ross attempts to bring the questions presented in its Petition within the realm of reviewability by claiming both that there is a relevant split in the circuits and by insisting that the decision of the Illinois Supreme Court conflicts with the majority of cases following one branch of that split. These assertions have no merit.

The "split in the circuits" alleged by Touche Ross is both non-existent and irrelevant. First, Supreme Court Rule 10.1(a) has no application here. Supreme Court Rule 10.1(a) states that certiorari may be granted based on a split in the circuits "[w]hen a United States court of appeals has rendered a decision in conflict with the decision of another United States court of appeals on the same matter . . . " Here, there is no federal decision even being considered as in error, and therefore no "split" as envisioned by this Rule can exist. Moreover, there weren't "alternative, independent" grounds for the federal court's rulings here, and thus the nuances of federal preclusion law raised by Touche Ross have no application. The only basis for the dismissal of the aiding and abetting claims against Touche Ross was the fact that the federal court found no primary securities law violations. (App. A-12, 13). A simple review of the federal district court and Seventh Circuit opinions on this issue confirms this conclusion was correct. (App. C-6; E-12). Those brief opinions make clear that, contrary to Touche Ross' assertion, there were no "independent, alternative holdings supporting the federal judgment" in its favor on the federal aiding and abetting claim. (Pet. at 22).

Nor did the Illinois Supreme Court rule that it was denying preclusive effect to the federal court's holdings because they were reached in the alternative, as Touche Ross contends. (Pet. at 24). The Illinois Supreme Court never declined to apply collateral estoppel because the alleged federal findings were reached in the alternative. (App. A-10-15). Touche Ross' assertion that the Illinois Supreme Court's decision implicates a split in the federal circuit courts on the issue of whether preclusive effect

must be given to "independent, alternative holdings" (Pet. at 24-27) is completely without merit.

Equally, there is no "state court of last resort [having] decided a federal question in a way that conflicts with the decision of . . . a United States court of appeals" as required by Supreme Court Rule 10.1(b). The Illinois Supreme Court was never asked to and therefore did not make a decision as to any federal questions. It would therefore be impossible to suggest that a reviewable issue exists under this Rule by virtue of anything that was actually decided by the Illinois Supreme Court. Nothing that was actually decided by the Illinois Supreme Court is in conflict with any collateral estoppel decision of a federal court of appeals.

B. Applying the Law as Requested by Touche Ross Would Not Alter the Illinois Supreme Court's Opinion

Review of this matter on certiorari would unnecessarily burden this Court's resources because applying federal common law, as now advocated by Touche Ross, would not alter the Illinois Supreme Court's opinion. Three elements for collateral estoppel application are common to both federal and Illinois law: (1) the issue decided in the prior must be identical with the one presented in the case in question; (2) there must have been a final judgment on the merits; and (3) the party against whom the estoppel is asserted must be a party, or in privity with a party, to the prior adjudication. (App. A-11; *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326, n.5 (1979);

Montana v. United States, 440 U.S. 147, 153-55 (1979); *Ballweg v. City of Springfield*, 114 Ill.2d 107, 113, 499 N.E.2d 1373, 1378 (1986).

There has been express recognition by this Court of a fourth element for federal collateral estoppel application: the issue decided in the prior adjudication must have been "necessary" to the decision in that case. *Parklane Hosiery*, 439 U.S. at 326, n.5. Thus, federal law limits collateral estoppel to those identical issues previously decided that were also "necessary" to the decision in the prior adjudication – Illinois law generally applies no such restriction.[6]

In applying collateral estoppel principles, however, the Illinois Supreme Court did apply the fourth federal element in reaching its decision. As the Illinois Supreme Court noted: "The doctrine of collateral estoppel applies only to controlling facts or questions *material* to the determination of both causes." (App. A-12) (emphasis added). In the next sentence of its opinion, the Illinois Supreme Court described this requirement as an inquiry into whether the issues "were *necessary* to the Federal adjudication" (*Id.*) (emphasis added). That is precisely the same standard identified by Touche Ross as the final requirement for federal collateral estoppel. The Illinois Supreme

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[6] The inclusion of this fourth element may account for Touche Ross' reliance upon Illinois law in its arguments to the Illinois courts, and its failure to assert below that the Illinois Supreme Court should have applied federal collateral estoppel principles. Illinois principles were clearly more advantageous to Touche Ross than federal common law.

Court in fact applied the very same principles that Touche Ross claims it should be required to apply under federal common law.

C. The Illinois Supreme Court Correctly Determined That Collateral Estoppel Did Not Bar the State Court Litigation Against Petitioner

The Illinois Supreme Court treated the federal adjudications as having potential collateral estoppel effect. After careful and thoughtful review, the Illinois Supreme Court correctly determined that collateral estoppel did not bar the Congregation's state law claims against Touche Ross. In so ruling, the Illinois Supreme Court first noted that the federal courts had not in fact addressed the merits of the Congregation's state law claims. (App. A-10). The Illinois Supreme Court next carefully considered each of the specific "findings" Touche Ross claimed should collaterally bar the Congregation's state law claims. After thorough review, the Illinois Supreme Court, found that most of the "findings" Touche Ross claimed were made by the federal court were simply not relevant to the state law negligence and breach of contract claims and therefore could not bar these claims. (App. A-12). In its analysis of these "findings", the Illinois Supreme Court described the distinction between the federal securities law claims that were decided by the federal courts and the undecided state law claims. The federal claims related solely to alleged Rule 10b-5 violations by others and Touche Ross' alleged role as an aider and abetter of these violations. The state law claims, by contrast, address the issue of whether Touche Ross could be held primarily liable to the Congregation, based on its

negligence or breach of contract, "for the manner in which [it] recorded the Newell investments in plaintiff's financial report." (*Id.*) The Illinois Supreme Court noted that the Congregation had retained Touche Ross as an "outside specialist" for the purpose of valuing Newell's investments, and that it was Touche Ross's inadequate performance of that outside accounting role that gave rise to the state law claims:

> [P]laintiff retained defendant to value Newell's investments. The district judge acknowledged that plaintiff could obtain review of Newell's investments by an outside specialist, and it is the asserted negligence of the outside specialist retained for that purpose – defendant, Touche Ross – that is at issue here.

(App. A-14).

Touche Ross was not hired to make investments or to recommend them, but to accurately report the value of the investments made by Newell and others. The state court was asked to decide whether Touche Ross made negligent misrepresentations about the value of the securities selected by Newell, or breached its contractual obligations to report those values correctly, and whether such negligence or breach of contract was a proximate cause of the Congregation's injuries. Touche Ross' obligations to value those securities accurately was completely separate from the issues of (i) who made those investment decisions, (ii) the authority the Congregation granted to Newell to make investments, or (iii) Newell's or the Congregation's general knowledge of the particular transactions or the Congregation's ability to track the paper flow generated by Newell and the dealers. The

Illinois Supreme Court therefore correctly determined that the federal findings as to Newell and his relationship with the Congregation were not relevant to the different issues raised by the state law claims against the accountants. (App. A-12).

As to other "findings" claimed by Touche Ross as having been made by the federal courts, the Illinois Supreme Court correctly determined that they had not actually been made by the federal courts. (App. A-12). For example, Touche Ross asserted before the Illinois Supreme Court, as it has here, that the federal courts determined that "Touche Ross had made no misrepresentations to the Congregation" and "that Touche Ross and the Congregation had agreed that the arbitrage investments would be reported at cost." (See e.g. Pet. at 22). In fact, as we have seen, no such findings were ever made by the federal courts. The Illinois Supreme Court got it right when it found that these and other purported findings were not "actually decided in the Federal adjudication" or were "clearly taken out of context when applied to plaintiff's relationship with defendant." (App. A-12,15). Not having been actually decided, these and other alleged findings could not have been "necessary" to the federal court judgments, and were not entitled to collateral estoppel effect. (App. A-12,13). The conclusion of the Illinois Supreme Court as to the collateral estoppel effect, or lack thereof, of the prior federal adjudication was correct under either federal or state collateral estoppel law principles.

CONCLUSION

For the reasons set forth herein, the Congregation requests that the Petition be denied.

Respectfully submitted,

THOMAS P. WARD
(*Counsel of Record*)
MCBRIDE, BAKER & COLES
500 West Madison Street
Chicago, Illinois 60606
(312) 715-5700

DAVID C. GUSTMAN
THOMAS KOTTLER
FREEBORN & PETERS
311 South Wacker Drive
Suite 3000
Chicago, Illinois 60606
(312) 360-6000

Attorneys for Respondent,
Congregation of the Passion, Holy Cross Province

Dated: September, 1994

Supreme Court, U.S.
FILED
OCT 5 1994
OFFICE OF THE CLERK

(3)

No. 94-341

IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

TOUCHE ROSS & CO.,
Petitioner,

v.

CONGREGATION OF THE PASSION,
HOLY CROSS PROVINCE,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of Illinois

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

FRANCIS J. HIGGINS
(Counsel of Record)
JOHN J. VERSCAJ
BELL, BOYD & LLOYD
Three First National Plaza
70 West Madison Street
Suite 3000
Chicago, Illinois 60602
(312) 372-1121

Attorneys for Petitioner Touche Ross & Co.

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Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of Illinois

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

Touche Ross & Co. ("Touche Ross") respectfully submits this reply brief in support of its petition for issuance of a writ of certiorari to review the decision of the Supreme Court of Illinois in *Congregation of the Passion, Holy Cross Province v. Touche Ross & Co.*, 159 Ill. 2d 137, 636 N.E.2d 503 (1994), *reh'g denied.*

I. The Petitioner Repeatedly Pressed and the Illinois Courts Passed Upon the Federal Question Arising From The Federal Courts' Judgments.

The principal argument posed by Respondent Congregation of the Passion, Holy Cross Province (the "Congregation") in opposition to Touche Ross' Petition for a Writ of Certiorari (the "Petition") is that Touche Ross did not "press" *constitutional* issues upon the Illinois courts in urging that they accord preclusive collateral estoppel effect to the determinations of the United States District Court for the Northern District of Illinois and the Seventh Circuit Court of Appeals. (Brief in Opposition at 18-22.) But the "pressed or passed upon" rule invoked by the Congregation[1] simply contemplates that Touche Ross press the *federal question* upon the state courts, not that the question be framed in federal constitutional terms. This Court, in granting certiorari petitions to review the failure of state courts to honor federal judgments, has clearly and uniformly held that the preclusive effect of a federal judgment is itself a "federal question" and has stated that "pleading a federal decree as *res judicata* in a state suit raises a federal question reviewable in this Court under [a predecessor to 28 U.S.C. § 1257(a)]." *Toucey v. N.Y. Life Ins. Co.*, 314 U.S. 118, 129 n. 1 (1941), citing *Dupasseur v. Rochereau*, 88 U.S. (21 Wall.) 130 (1875); *Deposit Bank v. Frankfort*, 191 U.S. 499 (1903); *Virginia-Carolina Chemical Co. v. Kirven*, 215 U.S. 252 (1909); and *Stoll v. Gottlieb*, 305 U.S. 165, 167 (1938), *reh'g denied*, 305 U.S. 675 (1938).

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[1]The Congregation repeatedly invokes what it characterizes as the "pressed *and* passed upon" rule, and asserts that this "rule" requires that a federal question be both raised and affirmatively decided below. However, "this rule operates (as it is phrased) in the disjunctive, permitting review of an issue not pressed so long as it has been passed upon ..." *United States v. Williams*, 112 S.Ct. 1735, 1738-1739 (1992).

By presenting the federal judgments and determinations to the Illinois courts and urging upon them the need to give preclusive effect to these federal determinations, Touche Ross "pressed" this *federal question* on numerous occasions at every level of the Illinois court system. The Illinois courts "passed upon" this federal question by expressly refusing to honor the federal court determinations. (In accordance with Supreme Court Rule 14.1(h), Touche Ross' Statement of the Case specifies each stage in the proceedings in which this federal question was raised, the manner in which it was raised, and the way in which it was passed upon by the trial court, the appellate court and the Supreme Court of Illinois, supported by specific references to the record.)

The Congregation likewise suggests that Touche Ross cited Illinois precedents below in asking that the Illinois courts give collateral estoppel effect to the federal determinations. (Brief in Opposition at 17). This, of course, is true, but Touche Ross *also* cited federal precedents to support that position, including *Lytle v. Household Mfg., Inc.*, 494 U.S. 545, 553 (1990); *Parklane Hosiery Co. v. Shore*, 439 U.S. 322 (1979); *Amoco Oil Co. v. Johnstone*, 856 F.2d 967, 969 (7th Cir. 1988), *cert. denied*, 490 U.S. 1046 (1989) (Brief of Appellant Touche Ross & Co. filed May 5, 1992 at 28-29 and 38) and *Schellong v. U.S. Immigration and Naturalization Service*, 805 F.2d 655 (7th Cir. 1986), *cert. denied*, 401 U.S., 1004 (1987), *reh'g denied* 482 U.S. 921 (1987) (Petition of Defendant-Appellant Touche Ross & Co. for Rehearing filed May 12, 1992 at 15).

Touche Ross argued to the Illinois Supreme Court that the federal determinations were dispositive of the Congregation's claims under both federal and Illinois law (as it stood at the time), but that the issue was "ultimately of constitutional dimension for the constitutional judicial power of the United States, the necessary and proper clause and the Supremacy Clause require

that state courts give full faith and credit to the judgments of the federal courts and this extends to the collateral estoppel effects of those judgments." (Brief of Appellant Touche Ross & Co. filed May 5, 1992 at 39, n.20.)

Touche Ross has not, as the Congregation asserts, espoused the "polar opposite" of the theory that prevailing federal law is inconsistent with the view of collateral estoppel "espoused" by the Illinois Supreme Court in the present case. (Brief in Opposition at 19.). Until the Illinois Supreme Court's surprising decision below, the Illinois law of collateral estoppel was identical to the prevailing federal law. In this case, however, the Illinois Supreme Court held, for the first time, that it would not give collateral estoppel effect to alternative federal findings, an approach totally inconsistent with federal law as articulated by most Circuits.[2]

II. The Supreme Court of Illinois Refused to Accord Collateral Estoppel Effect to Independent Alternative Determinations of the Federal Courts.

The Congregation states that the Illinois Supreme Court specifically held that the federal courts did not decide that "Touche Ross had made no misrepresentations to the Congregation," and thus did not decline to give collateral estoppel effect to such a determination. (Brief in Opposition at 29.) This is simply wrong. The Illinois Supreme Court did not deny that the federal courts had found that Touche Ross made no such misrepresentation.[3] The Illinois Supreme Court instead expressly held that, once it was

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[2]The court has recognized that even where a party has failed to press an issue in the proceedings below (which is *not* the case here), review by writ of certiorari is available when a court has disposed of a case on the basis of a new rule not addressed by the parties. *United States v. Williams*, 112 S.Ct. 1735, 1739 n. 2 (1992).

[3] The Seventh Circuit specifically stated that "[t]here simply were no misrepresentations made by the defendants to the Congregation." (800 F.2d at 182; App. E-8.) Touche Ross was a defendant.

determined by the federal courts that there was no primary violation of the securities laws, "any misrepresentations by defendant to plaintiff were not *relevant to the Federal claims*". (emphasis added.) (159 Ill.2d at 154; App. A-13.)

The Congregation also suggests that, according to the Illinois Supreme Court, the Seventh Circuit did not find that the Congregation and Touche Ross jointly agreed to the accounting treatment of the Newell positions. (Brief in Opposition at 29). But the Seventh Circuit, after finding that the decision was arrived at by Touche Ross after "consulting" with the Congregation, went on to find that the accounting treatment was spelled out in a footnote to the Congregation's own financial statements. Under the contract with Touche Ross, these were "the representations of management". The federal court clearly concluded that the parties *had* agreed on this accounting treatment. (800 F.2d at 184; App. E-13.) The Illinois Supreme Court did not deny that the federal courts found that such an agreement had been reached, but instead held that the finding was not "necessary to the federal adjudication", thus refusing to give effect to these alternative determinations. (159 Ill.2d at 153; App. A-13.)

III. The Dismissal Without Prejudice of the State Law Claims Does Not Negate the Collateral Estoppel Effect of the Federal Decisions.

Evidencing the same confusion about collateral estoppel as the Illinois Appellate Court (a confusion which the Illinois Supreme Court itself noted), the Congregation argues that collateral estoppel effect cannot attach to any of the prior federal determinations because the Congregation's state law *claims* were dismissed by the federal district court without prejudice. (Brief in Opposition at 27-28.) That dismissal is entirely irrelevant to the collateral estoppel issue. To argue otherwise, as the Congregation does, is to confuse *res judicata* (claim preclusion) and collateral estoppel (issue preclusion). Collateral estoppel applies to findings

and determinations where the "claim" or cause of action is different. The Illinois Supreme Court, in rejecting the very argument which the Congregation now resurrects, stated:

> While the Federal Court's dismissal of plaintiff's state law claims against defendant was not a final judgment on the merits, collateral estoppel could apply to findings made by the Federal Courts while ruling on the security (sic) law claims. . . . Plaintiff, therefore, is precluded from relitigating any findings that were made during the Federal Court's adjudication of the security (sic) law claims. (159 Ill.2d at 152; App. A-11.)

In short, despite the Congregation's efforts to bowdlerize the federal court opinions, it cannot be denied that both federal courts found *in the alternative* that: (a) there was no primary securities law violation to aid and abet and; (b) *in any event*, Touche Ross had not done what the Congregation alleged—misrepresent the value of the Newell arbitrage positions. It was the *second* alternative which the Illinois Supreme Court refused to honor, in contravention of federal principles requiring that such determinations be given preclusive effect.

CONCLUSION

Petitioner Touche Ross & Co. accordingly requests that a writ of certiorari issue to review the decision of the Illinois Supreme Court and that upon such review, the decision of the Illinois Supreme Court be reversed with instructions that judgment be entered for Touche Ross & Co. or, in the alternative, with instructions that upon retrial, Touche Ross shall be entitled

to an order collaterally estopping the Congregation from denying the matters determined against it in the federal court litigation.

Respectfully submitted,

Francis J. Higgins
(Counsel of Record)
John J. Verscaj
BELL, BOYD & LLOYD
Three First National Plaza
70 West Madison Street
Suite 3000
Chicago, Illinois 60602
(312) 372-1121

Attorneys for Petitioner
Touche Ross & Co.

Dated: October 5, 1994